



# A HANDBOOK OF ECONOMICS \* \* \*

G. M. NEMAWARKER, B. A.

SHAH & COMPANY,  
EDUCATIONAL BOOKSELLERS,  
AGRA



A  
HAND-BOOK OF ECONOMICS  
FOR  
INTERMEDIATE STUDENTS

*(According to the Syllab )*

WITH SPECIAL REFERENCE TO PORTIONS OF INDIAN ECONOMICS  
CONTAINING QUESTIONS AND REFERENCES TO  
THEIR ANSWERS IN THE BOOK

*By*

G. M. NEMAWARKER, B. A.,

---

*Published by*

R. S. DATE, B. A.

34, JUNA TOPKHANA, INDORE

---

**SHAH & COMPANY,**  
EDUCATIONAL BOOKSELLERS,  
AGRA.

# CONTENTS.

CHAPTER	PAGES
I Introductory	1
II. Economic Activities	3
III Production	5
IV The Factors of Production	10
V Capital and Organisation	24
VI Exchange	36
VII Money and Banking	46
VIII Distribution	67
IX. Interest and Profits	87
X Consumption	100
XI Spending and Saving	111
XII Taxation	115
Appendix. Questions	125

## BOOKS REFERRED

1	PENSON	Economics of Every day Life, Parts 1 & 2
2	MARSHALL	Economics of Industry Principles of Economics.
3	CHAPMAN	Outlines of Political Economy
4	MORELAND	Introduction to the Study of Economics for Indian Students
5	SELIGMAN	Principles of Economics
6.	NICHOLSON	Principles of Economics.
7	PANERJEA	Indian Economics
8	KALE V G	Indian Economics

## ERRATA

Page.	Line.	For	Read
1	6	ot	not
3	12	has	had
8	1	der	trader
8	2	Read "is" before "a"	
13	20	in 'general'	'in general'
21	22	sparecelly	sparsely
24	9	requisites	requisite
24	20	any	very
25	18	agent	agents
26	2	high waymen	highwaymen
26	7	cause	causes
28	11	that	than
28	23	wich	which
35	16	Chngea	Changes
44	12	Export	Exports
45	16	positions	position
46	16	standing	studying
52	28	metalic	metallic
57	18	rate	ratio
59	1	confussion	confusion
64	18	than	then
67	7	land	hand
75	23	X G F'	X G' F'
85	19	language	language
89	18	cereმოal	cereemonial

## Preface.

THIS little book is designed to meet the requirements of the students preparing for the Intermediate Examination in Economics of the U. P. Board and the Nagpore University. It covers the whole of the syllabus including the portions on Indian Economics. In writing a book of this kind it is impossible to be original. Hence the author has thought it wise to follow the main outlines of Penson's Economics of Every Day Life which is one of the Text Books prescribed. No pains have been spared to make the subject as simple and intelligible as possible. The aim and purpose of the author will be fulfilled if the book proves of any use to those for whom it is mainly written.

The author wishes to acknowledge his debt to Messrs. S. M. Samvastar, B. A., R. S. Date, B. A., W. R. Bhalerao and V K Dongre, for the help they have rendered him from time to time.

In conclusion the author is much obliged to Messrs. Shah and Company, Educational Book-sellers of Agra for successfully carrying out the printing work.

INDORE :  
15th July 1925. }

**The Author.**



Dedicated,

To

The Sacred Memory

Of

My Revered Mother.

## CHAPTER. I.

### INTRODUCTORY.

**Definition.** When we begin the study of a subject, it is usual to frame a definition of it. But the beginning is not the point where we can frame a satisfactory and an easily intelligible one. For the very terms in which it will be expressed will not convey their full meaning and significance to the reader, unless and until he is familiar with their whole scope and bearing on the subject

Economics is a subject which is full of such terms. There are terms with manifold meanings. For example, the term, "Wealth" in the ordinary sense includes all the material possessions, but in Economics its use is restricted to "all desirable things which satisfy human wants, and which are scarce and exchangeable" We have taken this word because it is with this word that Economics is sometimes defined. It is known as the *Science of wealth*.

In spite of the above difficulties in our way, we shall proceed with the definition given by Marshall. He says "Economics is a study of men as they live and move and think in the ordinary business of life." What we study is **Man**, a real human being. The definition of Economics as being the study of wealth is erroneous in as much as it overlooks the importance of the *Human Element* which earns wealth

(1) **Economics, A Social science** It would be out of the province of an elementary treatise



to discuss the claims of Economics to be reckoned either as a *Science* or an *Art*. We know that it is a Social Science. For each of man's activities, moral, juridical, economical, and political, there is a different science known respectively as *Ethics*, *Law*, *Economics* and *Politics*. Economics, it is said, is a part of the wider science of *Sociology*. We will now see what relation Economics bears to these and other sciences.

(2) **Economics and physical sciences.** Economics is only indirectly concerned with physical laws. It does not try to establish them. It is sometimes concerned with physical laws as premises, but never as conclusions.

(3) **Economics and Ethics.** There are two kinds of sciences *viz*, *positive* and *normative*. Positive sciences deal with the facts of the Universe as they are. While, normative sciences deal with the ideals of facts. Ethics is a normative science, in as much as it lays down what conduct ought to be and not what it is. Ethics has a very partial relation to economics. A man does not work only for his own selfish motives. There are present the sense of duty, love of family, and a sympathetic attitude towards other human beings. These motives are ethical as well as economical.

(4) **Economics and Politics.** Economics is concerned with man in his social as distinguished from his political relations, and it is in certain departments of economics that we are concerned with men in their special character as members of State—*Public finance*. But there are many points of contact between Economics and Politics, and in its practical

aspect the connection between the two is very intimate.

(5) **Economics and Sociology.** Sociology has been defined "as a study of the natures and activities of individuals regarded as members of communities, and the relations between them" (Chapman). It is said that the complicated phenomena of wealth can not be studied apart from other aspects of social life Economics thus becomes a branch of sociology.

## CHAPTER II.

### *ECONOMIC ACTIVITY.*

(1) The chief cause of man's activities is that he has wants. These are numerous and manifold in nature. In the primitive ages the savage has very few wants. His want was for a morsel of meat, which he satisfied by killing wild animals. But to hunt them he had to make tools. Thus each recurring want required a corresponding effort on his part. The first stage of economic life is this, that wants call forth an effort which results in the direct satisfaction of the want.

(2) **Indirect effort.** As men progress in civilization, they know advantages of pursuing different kinds of trades. They distribute among themselves the various kinds of work. A person who is ill and can not go to the forest for hunting, will prepare say, tools, or do some other kind of work at home. Indeed, his wants are not to be

satisfied directly by doing this kind of work but he will have to find out some person who is ready to exchange say, meat for these tools. Thus he has satisfied his wants directly. This, then is the *second stage* of development. The characteristic of this stage is the division of labour. Therefore it leads to barter, that is to say, exchange. The division of labour, however, is such that each man works independently in producing an article. A man had to do the work of barter before he could satisfy his wants. Barter is nothing more than exchange of one thing for another

(3) **Third stage** In this stage man has advanced much further than he was before. He has learnt to combine in group or to co-operate with others to satisfy his wants. As an illustration of this, we will take the construction of a canoe. "Here, instead of a single man working out a canoe, there is a group of three or more. One has felled the tree. Another has prepared the wood, and a third will perhaps do the covering and a fourth may do the actual construction." Here we find that these men had wants and their combined effort has produced a certain thing which will indirectly satisfy these wants. The characteristic of this stage is distribution which results from co-operation or association of the workers into groups, and which comes after exchange or barter of the joint-product. In the illustration given above, we see that the individuals who worked out the canoe, get it exchanged for corn. A new difficulty now arises as regards the possession of this corn. Who is to take the corn? This brings us to the process

known in Economics as *Distribution*. The corn is to be distributed among these persons

(4) **Fourth stage.** In the primitive stages exchange was effected by barter. But modern life with all its complexities presents altogether new difficulties which barter can not remove. We will understand this well if we illustrate these difficulties by an example. Suppose a man has, say, wood with him, and is in need of corn. He must find out a person who has corn to spare and is also in need of wood. In short, there must be the double coincidence of barter. In order to obviate these difficulties, money has been introduced. Whatever a person produces is expressed in terms of money income. An intermediary is thus introduced between wants and their satisfaction. It is income which is spending power and a man spends as much as his income will allow him to do. The characteristic of this stage is the introduction of money, thus splitting up exchange by barter into two parts. One of which called sale comes before distribution and the other which is called purchase comes after distribution.

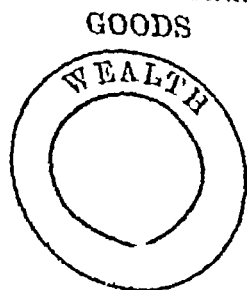
---

## CHAPTER III.

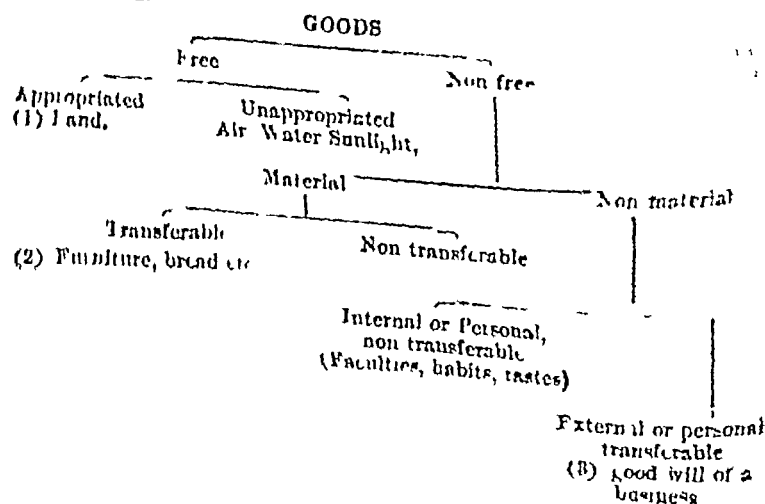
### PRODUCTION

(1) **Wealth and Goods** In the previous chapter we have seen that economic effort was chiefly directed towards the production of wealth. In order to understand this statement we must see what wealth and production mean. Wealth in the ordinary sense of the word means material possessions.

of different kinds. When we speak of the wealth of a person, we include in it his land and house, his carriages, his money and other household goods. We must take precaution to distinguish goods from wealth. "Goods are all desirable things, all things that satisfy human wants." As wealth also satisfies wants, it is desirable. Therefore wealth consists of those things which satisfy human wants and are desirable. Hence all wealth consists of goods but not all goods are considered as wealth. We will illustrate this distinction by a diagram.



Wealth is a smaller circle, forming part of a wider one of goods. Some goods are wealth while all wealth is goods. In the following table an attempt has been made to give the different classes of goods.



From the above table it will be quite easy to find out what goods are wealth and what are not. Those which are marked (1), (2) and (3) are *economic goods or wealth*.

It is certain that both wealth and goods possess utility which is the power to satisfy wants. Wealth is distinguished from goods by two more differentiating attributes which are scarcity and exchangeability. We will cite a better definition of wealth from the strict economic point of view. "Wealth consists of all goods, material and non-material which satisfy some human want, which are not supplied by nature in such abundance as to satisfy all human wants in regard to them, and the ownership of which can be exchanged" (Dr. P. Basu).

(2) **Production defined.** Let us now turn to the meaning of production. "Man" says Dr. Marshall "cannot create material things." "He only changes the form or arrangement of matter to make it convenient to satisfy his wants" It is sometimes said that a trader does not produce anything. He only sells things produced by others. But it is not true. Although the trader has not produced the coin himself, he has no doubt created a utility in bringing it to a place where it would find purchasers. Here we are introduced to three kinds of utilities. They are *form* utility, *place* utility and *time* utility. The carpenter who makes a chair out of a log of wood is said to create form or shape utility. The furniture dealer who takes the chair to the market creates place utility. A

trader who stores up corn for selling it when there is a great demand for it creates a time utility.

(3) **Productivity of labour.** We have seen throughout our survey of wants and their satisfaction that there is an effort on the part of man. In other words he performs some sort of labour. There is a difference of opinion amongst writers on economics regarding the productivity of labour. Some say that labour is to be judged from two stand-points viz (I) Productive and (II) Unproductive. Others do not attach much importance to this distinction. We know that all labour contributes towards producing some effect. We should then say with Dr. Marshall that 'It would be best to regard all labour as productive except that which failed to promote the aim towards which it was directed and so produced no utility.' Nothing depends upon the productivity or unproductivity of labour. We must keep our attention on the degree of productivity. It is the amount of produce and not mere produce which matters most. The differences in the degree of productive effort play an all important part in the social and economic condition of individuals and of nations. They, therefore, deserve careful study.

(4) **Productive effort.** The nature of productive effort is to be studied from three points of view (1) the combined productive effort of many groups (2) the productive effort of a particular group (3) the productive effort of an individual worker

(I) It includes the sum total of all the efforts undertaken with a view to satisfy wants. There

is no organization among the groups. Each is working for his own wants, quite unconscious of the fact that his effort is a sort of contribution to a much wider effort.

(II) This is distinguished from the previous group by (1) division of labour being arranged on a definite plan, and (2) the co-operation being effected deliberately. There are six types of industrial groups of this kind. They are respectively engaged in (a) farming or commerce (b) manufacture (c) transport (d) commerce (e) financial matters (f) retail trade. These no doubt differ much in size and composition. There are certain features common to all these types. (i) The group has got the employers, capitalists and labourers who strive for the prosperity of their business as a whole and for the reward of the services rendered by them. (ii) In every group there is the organiser who directs and controls the efforts of the individual members of the group.

(III) Although the output of an organised group is due to the combined efforts of many, yet a single individual has also contributed to the quality and quantity of that output. The character of an individual plays a great part in the prosperity of a business. There are two features of the individual's work. (i) The dependence of one member upon another. Both the employer and the employee are dependent on each other: the former for the efforts of the latter, who in turn require the careful organising capacity of the former. Besides, an individual can not do his work unless



some one has supplied him with the necessary materials. (Students should take a careful note of the example cited by Penson). (ii) The work of each is incomplete. An employee cannot say that he has prepared a certain thing solely by himself. He has only contributed in a partial measure towards the preparation of that thing. Let us take the well known example of pin-making as given by Adam Smith, the founder of Economic Science. "One man draws the wire; another straightens it; a third cuts it, a fourth points it, a fifth grinds it at the top to receive the head". Thus each person has contributed some effort towards the completion of a pin.

## CHAPTER IV

### *THE FACTORS OF PRODUCTION.*

The absolutely necessary agents of production are (1) Land (2) Labour and (3) Capital. Some regard organisation as the fourth agent of production. We will understand the meaning of each of these well if we study them separately.

(1) **Land** The term land as used in its strictly economic sense includes more than the surface of the earth which we see. It is to be understood comprehensively to denote the whole animate and inanimate nature excluding human beings—nature which is of any economic use. Dr. Marshall's definition of land is very useful and requires mention. "By land is meant not merely land in the strict sense of the word but the whole of the material and forces which nature gives

reely for man's aid, in land and water, in air and light and heat." Land is generally distinguished from capital as a separate factor of production. It is claimed for instance, that land is a gift of nature while capital is product of labour. Again, land is indestructible while capital is perishable. But this distinction says Dr Marshall is a "Loose one". The qualities which give value to the land are not indestructible. The chemical ingredients require often to be renewed. The only distinguishing feature of things classed as land is that men can not increase their quantity.

Land has a value as a factor of production because it yields some concrete produce. The productivity of land depends upon two essential qualities *viz.* (i) Fertility and (ii) Situation

(2) **Fertility.** We see that every land does not yield a good produce. There are certain lands which contain soils that are most fertile, while there are others which are nearly barren. Man has succeeded in having a control over the character of land. He can make some lands yield large amount of produce. He has studied the properties of each soil, and has found out the requirements of each. By certain chemical artifices he can permanently change the character of a land. We must here note in particular the 'original and indestructible properties of land' as Ricardo called them. These are the annuity that nature has given it of sunlight, air and rain. It is on these that the fertility of land depends. It is true that human beings can make a land yield as greater a produce as they can. But there is a check put to their

efforts by what is known in Economics as the law of *Diminishing Returns*.

(3) **Law of Diminishing Returns.** In agricultural land there is at every time a maximum return from the application of capital and labour. This application of capital and labour is called a 'Doze'. The dose which just compensates the cultivator may be said to be the *marginal dose* and the return to it the *marginal return*. When we apply a dose to the land which just pays its expenses, we mean that we have applied it to the land which is on the *margin of cultivation*. With these preliminary notions we shall now turn to the meaning of the law. Cultivators have learnt from experience that it does not pay to do more than a certain amount of work for any given crop grown on a particular quality of land. If they go on applying more and more doses of capital and labour to land, they will in the beginning get an increasing output, but a certain point will be reached when, the returns will be diminishing in proportion to the increase. Let us illustrate this point. Suppose that cultivators of a particular piece of land find that they get fifteen maunds of wheat from an acre when they have ploughed 8 times and irrigated 3 times. A particular cultivator now ploughs sixteen times and finds that he gets sixteen maunds of wheat as the result. That is to say eight additional ploughings have secured one additional maund of wheat. Does this pay him? It does pay him if he can get one ploughing done for less than five seers of wheat, for then the additional 8 ploughings have cost him less than  $5 \times 8$

= 40 seers. He will have spent more than he has gained, if a ploughing costs more than five seers. (Moreland). Thus a proportionate increase has for some time begun to give an increased output. But after a certain stage has been reached every succeeding dose has begun to yield a less than proportionate increase. We are now in a position to make a statement of the law. It is thus stated by Dr. Marshall. "An increase in the capital and the labour in the cultivation of land causes in general a less than proportionate increase in the amount produced, unless it happens to coincide with an improvement in the art of agriculture" If a proportionate increase in dose of capital and labour would have brought a proportionate increase in the amount raised, there would be no limit to expenditure on a given piece of land. But this is not so.

Now let us examine the statement of the law. We have the words in 'general' in it. It means that in particular cases, the law does not operate. An individual cultivator may have an increased output. But it cannot be true of all

The second limitation to this law is that its application is limited to a period during which the art of agriculture does not change materially. Although new improvements in the art of cultivation are introduced, it would be for a certain time that the return would be proportionately large, but the law will soon come into operation when a certain point is reached after which each succeeding dose of capital and labour will bring on a proportionately diminishing return.

(4) **Situation** We have so far been dealing with the fertility of land. Let us now consider the other requisite *viz.* situation. The value of agricultural land depends as much upon situation as it does upon fertility. A man who has land close to a large city will grow fruit and vegetables which he can sell much more than wheat and maize if grown on the same land. But in the country there is no market for these (fruits) products and consequently he will not grow them. A land may be very fertile, but it will have no value if it is situated in a wild jungle. In this respect it will be less valuable than an ordinary land which yields less produce but is situated near some market. As means of transportation increase day by day, the fertile lands which are situated in a far remoter area, are being gradually brought into contact with Markets. Railways have facilitated this to a much greater extent. Cultivators can increase the produce with certainty that the output would be taken to distant places where it would find good market.

Again, some lands enjoy the advantage of being in particular way situated near rivers or canals. If these be less fertile they can be made to yield good produce by irrigation. There are some fields which are near the village house and thus much easily manured than the fields at a distant

(5) **Natural Resources of India** India is a vast country and its geographical and climatic conditions vary from place to place. In the Punjab and United Provinces there are big rivers which are used for irrigating and fertilising vast areas.

The soils in one part are very rich while in others they are extremely poor. Owing to the variety of climatic conditions, the soil produces different kinds of crops. Gold, coal, petroleum manganese and iron are found in considerable quantities in some provinces. "The forest produce of India too is varied and rich and its economic possibilities are steadily being realized. Excellent qualities of timber, and fibres, grasses and distillation products, oil-seeds, tan and dyes, gums and resins, rubber, bamboo, canes, drugs and spices are found in these forests. Many of these products are calculated to supply raw materials for industries" (Kale V G.)

(6) **Soil and Climate.** The most extensive and important from the point of view of agriculture are the alluvial soils. They cover the greater areas of Sind, Gujrat, Rajputana, the Punjab, the United Provinces, Bengal and the extensive tracts in Assam and Burma, the Godavari, the Krishna and the Tanjore districts of Madras. These soils differ in different parts of the country. In some places we find soils which are porous and light. These are easily worked by the plough. In other places, they are non-porous and clayey. A large variety of *rabi* and *kharif* crops are grown on these soils.

Besides this, there are the black cotton soils, trap soils and the crystalline soils. The black cotton soils are generally found in the tracts of the Deccan, some districts of Bombay and also in some parts of Madras. The crops, usually grown on these soils, are wheat, cotton, linseed and millets. The crystalline soils are found in the whole of the

Deccan, Central Provinces, Hyderabad and Kathiawar. The chief crops grown are millets and pulses. The crystalline soils are most suited to the growth of rice. In general it may be said that these soils are dry. This absence of moisture in the land makes the supply of water an absolute necessity in the Indian agriculture.

(7) **Climate.** As the whole of the peninsula falls within the tropics, the climate is hot. It is no doubt true that there are variations in the climatic conditions of India. The Northern India being out of the tropic of cancer, the climatic conditions are very complex. In the Punjab and the North-Western Frontier Provinces, there is extreme heat in summer and bitter cold in winter. In Bengal and Assam the winter is mild and the summer is moderately hot. Sind, the Punjab and Rajputana are dry, while the atmosphere in Assam is saturated with moisture. India is chiefly an agricultural country. She has, therefore, to depend much upon the rainfall which is influenced by the configuration of the country. On the Eastern and the Western Ghats, there is a heavy rainfall owing to the south-west monsoons. And as rice requires a good deal of rain, we find that it is usually grown here in large quantities. The S. W. monsoons are very important in as much as they supply the major amount of rains to India. But the uncertainty of the rains here has had a great effect upon the agricultural conditions. Sometimes, there are no sufficient rains. As a consequence, the poor agriculturists are driven to starvation and poverty. But these difficulties are now being

ridden over by irrigation.

(8) **Labour.** To obtain the necessities of life, every living being is required to do certain amount of work. This work is known in Economics as Labour. It includes the work done by human beings but excludes that which is done by animals. When we speak of a labourer, we generally mean one who does manual work. We overlook the other essential quality of the labourer *viz.* his intellect. A person would at the first instance be puzzled to hear of the intellect of the labourer. But we know that there are certain kinds of occupations which require both the manual as well as the intellectual labour of a person. Much depends upon the efficiency of labour in production. We will therefore make a careful study of this factor.

(9) **Efficiency of Labour.** If we suppose that the supply of the other factors of production is constant, we will find that the amount of produce raised will depend upon the number of labourers. Indeed, it will not do to have a large number of labourers merely. A small number of skilled labourers would produce much more than a large number of lazy and unskilled ones would do. The supply of labour comes from the population of the country. Hence a brief survey of population will not be out of place here.

(10) **Population.** For the study of population, we must go to Malthus whose Essay on population is the source of further thought upon the subject by the modern economists. Malthus' three propositions are:—



I. Population is necessarily limited by means of subsistence. These are "food, fuel, clothing, shelter etc."

II. Population invariably increases when the means of subsistence increase unless prevented by powerful and obvious checks. But the increase in the means of subsistence must be such as the mass of the people can command.

III. "These checks which keep the population down to the level with the means of subsistence are first (i) Positive *i.e.* those which increase the death rate *e.g.* Epidemics, wars etc. and secondly (ii) Preventive, those which diminish the birth rate *e.g.* moral restraint" (Nicholson). The substantial soundness of Malthus' main propositions is undisputed. But in detail he is open to criticism. For example, population does not always increase upto the limits of food. In considering the truth about the laws of population it should be remembered that (1) they were formulated at the time of great distress owing to French Wars, bad system of poor relief etc (2) that Malthus perhaps overestimated the potential rate of increase in population and underestimated the force of moral restraint (3) that he could not foresee the effects on food supply of free trade, cheap transport and modern industrial development. (Nicholson).

(11) **Density and Distribution of Population in India.** In the country taken as a whole, there are on the average 75 persons to a square mile. In British Territory the number of

square miles is 223 and in the Native States 100. The density of population varies in the different parts of the country and is dependent upon the climate, quality of the soil, rainfall and other conditions. The following table will show how the density varies in different provinces.

Province	Density per Sq Mile.	
Madras	...	291
Bombay	...	145
Bengal	...	551
United Provinces	...	427
Central Provinces	...	122
Burma	...	53
Punjab	...	117
Behar and Orissa	...	344

From the above table it is quite evident that where there is sufficient rainfall, there is a large number of people residing. The reason being that India is chiefly an agricultural country and her population is mainly dependent upon this industry. Hence where there are good facilities of increased production, we will find that there the number is the greatest. The population of this country is mainly rural. Only 9.5 p c of the population are found in towns with over 5000 persons each. There are only 30 towns with a population of over 100,000. But the number of villages is no less than 730,000.

**Distribution of Population.** The majority of the female sex is not to be counted as the producers of wealth. Only the females of Lower Classes do some work in the way of producing

wealth. Besides this there are the old and very young persons who do not contribute any thing to the country's production. Now the remaining persons are distributed into several occupations. Over 72 p c of the population of India earns its livelihood by agriculture. Industries maintain 11.2 p c and trade and transport 5.6 and 1.6 respectively. The rest of the people are engaged in the following occupations —

Professions and liberal arts	...	1.7 p c.
Domestic services	...	1.5 „
Public administration	..	.84 „
Public force	...	.77 „
Extraction of minerals	...	.17 „
Insufficiently described occupations		2.9 „
Unproductive occupations	...	1.1 „
Persons living chiefly on their incomes		.17 „

“In India it is true, British rule has abolished civil war, and total population has increased very rapidly during the last century as Railways, irrigation works and other modern innovations have added to the productive capacity of the country. But famine is still lamentably frequent and in spite of industrial progress it would seem to be true that the population readily rises upto the limits of the means of subsistence.” (Layton: Introduction to an Essay on population by Malthus). In the course of the last ten years (1911-21) the actual increase has been 3,918,736 or 1.2 per cent.

**Means of Communication and Transportation in India.** Roads were first construc-

ted in the Mohamedan rule. Since then the Government itself has made roads all over the Country connecting the chief towns. Besides these the rivers have been used as highways. The Indus, the Irrawadi, the Ganges and the Brahmaputra have been the chief means of inland navigation. These rivers carry on a greater portion of the internal trade of the country.

With the advent of the steam engines, Railways began to spread over the country. The first three lines were constructed for experimenting in 1845. These were (1) from Calcutta to Rangoon (E. I. Railway) (2) Bombay to Kalyan (G. I. P. Railway) and (3) Madras to Arkonum (M. S. M. Railway). Indian Railway building is said to have been carried on, on a serious scale during the regime of Lord Dalhousie. At the present day we find that nearly the whole of the Peninsula has been intersected by the network of Railways. These have provided many economic facilities. (1) They have decreased the cost of travelling and (2) Surplus population can be removed to sparsely populated areas. (3) They have helped manufacturers by cheap and quick transport.

**Irrigation.** We have seen while studying climate that rainfall in India is not sufficient to meet the requirements of the country. In some places there are absolutely very little rains, while on the Ghats and the coast strips, they are abundant. The deficiency of rains has been covered partially by irrigation. There are rivers like the

Indus, the Ganges the Jamna and Godavari which have been used for irrigating large and extensive tracts of the country. This has completely changed the condition of the agricultural lands here. Where there were barren and dry areas of lands lying useless, we find there green plains all cultivated and yielding a large amount of produce. There has been during the last forty years a steady growth in the area irrigated by Government. From 10.5 millions acres in 1878-79 the area annually irrigated rose to 19.25 millions acres in 1901 and to 28 millions acres in 1910-20. Out of the total cropped area only 14 per cent is irrigated. Irrigation is carried out on different lines in different places. There are first of all the inundation canals. Water is supplied to the fields by leading it from rivers and streams by means of inundation canals. These are mainly to be found in the basin of the Indus and its tributaries. Secondly there are the perennial canals. These are to be found in United Provinces, the Punjab and Madras. The important of these canals are the Jamna canal the Bari Doab canal (in the Punjab) and one in the delta of Mahanadi in Orissa. In the U. P. the Ganges and the Lower Ganges canals are the two principal perennial canals. Finally there are storage works. These are chiefly found in Bombay and Madras, for the rivers here have short courses and the rain which frequently falls in heavy but brief streams passes away rapidly. The Periyar system in the Madura district of Madras is the most interesting reservoir scheme in India.

(12) **Requisite of the efficiency of Labour.** The efficiency of labour depends upon (i) health and vigor (ii) skill and (iii) moral qualities.

(1) These generally depend upon the climate and surroundings of the labourer's residence. If the climate be too hot, it will exhaust the labourer's energy very much. The surroundings of a labourer's quarters play a great part in the moulding of his physique. If he works in the country where he gets ample fresh air and where his cottage is not situated in crowded locality, he will become strong and vigorous. But in a town where houses are crowded, it is very difficult to find much of open space and air. Factories are located in crowded places where the labourer's life simply rots for want of fresh air.

Much depends upon the quality of food too. "Food must supply the nitrogeous and other elements that are required to build up growing tissues and to repair the waste of body. It must also afford heat some of which must be capable of being converted into muscular force. And for this purpose carbonaceous food, when it can be properly digested, is the cheapest." (Marshall).

(2) **Skill.** A skilled labourer does more work in less time and that too quite to the satisfaction of the employer. It requires a good deal of training and practice in order that a labourer should be well skilled in a particular occupation, the illustration of a Potter given by Moreland is worthy of our attention. "The work of a Potter for instance looks very simple; he spins his wheel,

throws a *lump* of clay in it presses it with his hands, touches it with a knife and then as the wheel comes to rest, takes off the jar or cup which he has made and puts it with others to be *baked*." The author further remarks that if the spectator who is quite unused to this kind of work, were to take the Potter's place, he would not be able to do a jot of it. On the contrary he will confuse the whole thing. We then see that the chief requisites for the attainment of this sort of skill is practice. The potter has been watching his father work on the wheel and was under his training. Besides this, a labourer is required to use his discretion in some kinds of work, such as those in Factories.

(3). **Moral Qualities.** These include the labourer's regularity, honesty and diligence. If a labourer works hard and honestly he will no doubt do much work. He is often left alone to mind his own business where if he tittle with his job he will produce nothing or any little. In some businesses there are valuable materials which are supplied to the workman. If he is honest, he will be trusted otherwise he would be constantly required to be watched by the Manager.

---

## CHAPTER V.

### CAPITAL AND ORGANIZATION.

(1) **Capital:** Capital is generally defined as that part of a person's stock from which he expects to derive an income. It covers the materials a man has for use, the goods he has ready for sale,

the tools and machinery he uses and the money which he employs in paying wages and in other expenditure incidental to the process of production which he is carrying out. We must here distinguish between that part of a person's wealth which is capital and that which is not. Marshall has brought out this distinction very clearly. He says "We should use the word wealth in preference to capital when our attention is directed to the relation in which the stock of useful things stand to general well-being, to methods of consumption and to pleasures of possession; and that we should use the term capital when our attention is directed to those attributes of productiveness and prospectiveness which attach to all stored up fruits of human effort but are more prominent in some than in others. We should use the term capital when considering things as agent of production and we should speak of the term wealth when considering them as results of production, as subjects of consumption and as yielding pleasures of possession". Suppose a person has got 50 mds of wheat with him. If he stores this up with the intention to make good money out of it when it will have great demand, it will be a capital to him. While if he uses it for his own consumption, then it will be called wealth. The same thing may be capital to one and wealth to other. Thus a motor car will be wealth to a rich person who uses it for pleasure. On the contrary it is capital to a Doctor who rides it to visit his patients and thereby earns an income.

(2). **Growth of Capital.** In ancient times people did not save much capital because there



was no security that what one has saved he would be able to enjoy it. There were high waymen and robbers who were a constant source of trouble in this respect. Now as the world has progressed and there is the protection of the State, people are less in danger of losing what they have accumulated. It will be worth our while to study the cause that lead to the growth of capital in a country.

**Surplus Produce.** "The maximum that can be added to the material capital of any society during any period is the total net product i.e. the excess of produce during that period over what is needed to provide for the efficiency necessary of the workers and the supply of raw materials. In considering the causes that induce people to save rather than consume, we are concerned with the will to save. The actual saving effected during any period will depend upon two groups of causes:

Power to save depends upon all the factors of national production namely :—

(i) Natural resources and powers. (ii) Efficiency of labour (iii) The amount taken by Government for public purposes e.g. taxation. (iv) Indirect expenses e.g. restraint on trade. (v) The nature of expenditure of public revenue. (vi) Extent of foreign trade. (vii) Means of transport and communication (viii) The credit system of the country.

Will to save depends upon:—

(i) Security which includes (a) Security that which is saved will be preserved or enjoyed by the owner (b) Security afforded by state against violence or frauds, breach of contract on the part of individuals. (ii) Protection against the arbitrary exaction of the Government itself. (iii) Security against the violence and uncertainty of the powers of nature. The other factors are the affection for one's family, rate of interest and hope of rising in a social scale.

✓ (3) **Forms of Capital.** (i) *Consumption Capital.* "These consist of goods in a form to satisfy wants directly. These are food, clothes, house-room etc. (ii) *Auxiliary or Instrumental Capital.* This kind of capital consists of all kinds of goods that aid labour in production. These are tools, machines, factories, Railways and raw materials of all kinds (iii) *Circulating Capital* Capital which fulfils the whole of its office in the production in which it is engaged by a single use is known as circulating capital e.g. Raw materials, finished goods (iv) *Fixed Capital.* Capital which is capable of rendering repeated services is called fixed capital e.g. buildings, plant, machinery.

(4) **Organization.** We will study this factor on the following lines. (i) Influence of machinery on manual labour (ii) Division of labour. (iii) Localization of industries (iii) Large and small scale production

(A) **Machinery.** Every body knows that practice makes men perfect. A person becomes

quite an expert by doing the same thing many times. It then becomes a sort of routine work to him. But when it is so, it is better that it should be replaced by some more fruitful and easy method. Machinery has greatly substituted manual labour and that too to a great advantage.

*Advantages* — The advantages which are ascribed to the substitution of machinery are the following:—

(i) It can work faster than the human limbs can move.

(ii) It works more accurately than the human limbs, because it exactly repeats its movements; whereas even the most dexterous operative can not depend upon exactly repeating his movements.

(iii) It removes the barriers between different trades. Every where the machinery is generally the same. The difference is of a very slight degree, therefore a person who is working say, in a watch factory will readily adapt himself to the machinery in a knife factory if he is required to give up his former vocation.

(iv) It undertakes work which is beyond the strength of an average labourer. "The stupendous forces of Nature can be pressed into the service of man when engines exist to transmit them, and machines for them to drive." (Chapman).

(v) It removes monotony in work, that which is uniform and monotonous is gradually taken over by the machine, which thus becomes ster-

dily more automatic and self acting . till atleast there is nothing for the hand to do, but to supply the material at certain intervals and to take away the work when finished (Marshall).

**(B) Division of Labour.** When machinery was introduced, each individual was required to do a particular kind of work. This division can be effected in different ways. (1) In a village, people take up to particular industries. The wants of the people in it are satisfied by those who follow different vocations (2) Secondly there is another aspect of the division *viz* division into processes each complete in itself " At the present time boots are often made by hand, and in certain cases a single workman may do all the work himself, but for the most part boots are made in factories. The work is then divided up into several processes, each involving the use of a special type of machine. A worker becomes expert in a particular process " (Penson).

*Advantages :—*(i) Dexterity of the worker is increased through constant practice of the same thing.

(i) Workers can be classified according to their capacities and full employment can be given to the implements

(iii) Economy of time There is no waste of time in passing from one form of work to another, and in starting different operations.

(iv) Continuous specialization promotes the discovery of invention.

(i) Division of labour shortens the period of apprenticeship (Nicholson).

*Disadvantages.*—(i) Labourer's mind tends to grow narrower owing to the restricted character of his work

(ii) Excessive specialization of individual.

(iii) Monotony of constantly repeating the same process tends to intellectual dulness and inefficiency.

(iv) Evils of factory system indirectly tend to make labourers unhealthy.

(C) **Localization of Industries or Territorial Division of Labour.** There are many causes which have led to the localization of industries. The prominent among these are —

(i) The character of the climate and soil.

(ii) Proximity to the source of materials or powers provided by nature. Each industry tends to be established in one or more localities, and cities and towns become specially adapted to the needs of a particular industry. Thus all most all the Jute Mills in India are close to Calcutta. Bombay, Ahmedabad and Cawnpore are known as chief centres of cotton spinning and so on.

When an industry is once localized in a particular place, it is likely to stay there long for the following reasons'—

(1) Both labour and capital become specialized and there is a continuity of improvements.

(2) Industries grow up which are subsidiary to the main industry

(3) Means of communication are adopted both to the acquisition of raw materials and to the marketing of product. (Nicholson)

(D) Large and Small Scale Production.  
*Advantages --*

(1) There can be a better classification of labour according to its capacity

(2) Applied machinery can be so adjusted as to give full employment to the motive power

(3) Improvements can be more readily adopted.

(4) Small inventions can be encouraged.

(5) Expert skill (which is very costly) can be called into a greater extent.

(6) Better Agents can be employed in a selection of materials and of process.

(7) Better control of departments. One department can be put into hands of competent managers while the energies of the head of the department are devoted to general superintendence and organization.

(8) A large business deals in great quantities and therefore cheaply; it pays low freights and saves on carriage in many ways, particularly if it has a Railway siding.

(9) It often sells in large quantities and thus saves itself trouble.

(10) It often spends large sums in advertising by commercial travellers.

(11) It can make use of waste products

On the other hand, the small scale production offers advantages of its own.

(1) The small manufacturer saves in superintendence.

(2) He gains much from the modern diffusion of trade knowledge. Whenever there is any new invention in trade or industry, it does not remain a trade secret for the persons who make this; are generally students of science rather than traders. (Marshall).

There are the following limitations to production on large scale.

(1) Certain types of businesses are more successful on a small scale than on a large scale. As we have just seen the small manufacturer can superintend his work very carefully, for the success of an undertaking depends much on the personal attention of the employer to every detail.

(2) An increase in the scale of production is sometimes followed by a less than proportionate return. The second limitation is the law of Diminishing returns. We have studied (while studying the fertility of land) the operation of this law on agricultural lands. In manufacture this law operates for some time in the opposite direction. An increase in capital and labour brings in the advantages of division of labour and large scale production. The amount of output is increased in proportion to the increased application of capital and labour.

*Law of Increasing Returns.* The application of increased dose of capital and labour brings on other things being equal a more than proportionate return.

*Law of Constant Return.* It some times happens that the return neither diminishes nor increases but remains constant.

(3) The third limitation is the extent of market. The division of labour, as Adams Smith tells us, is limited by the extent of the market. The goods which are manufactured must find a market otherwise there is no use of producing them on a large scale. The manufacturer produces with the hope that what he produces will be purchased by the customers. He can lower the price (which a large scale manufacturer can conveniently do) and thus attract customers to his shop. He must produce those things only which have a general demand.

**(5) Development of Industrial Organization.** This has been very continuous and different in different countries. It, therefore, requires a brief survey.

*Self supporting groups.* "We mean by this stage that a group of people themselves produce all the things which they require and they obtain nothing from the group outside." (Penson.) In India we find many villages where this group system is still in vogue. Each village is a self-contained unit.

When the means of communication and transport increased people began to keep communication



with persons of other towns. There arose centres of trade and industry where labourers flocked in from neighbouring villages to earn their living; organisation began to be pursued on definite lines. From the town life we are brought to the consideration of various forms of industrial organisation.

*The Gilds* This system characterised the industrial life of Europe for several centuries. "With the increase of wealth, however, a twofold process went on. The gilds grew more grasping and exclusive, until they became monopolistic bodies proving a drag upon industry instead of a help. Membership was confined to a select few whose right to practise trade was inherited. Newer industries started whenever they could, independent of the crafts" (Seligman)

But the gilds gradually began to decline in importance. From this stage we now pass to the state regulation of Industry and Commerce, to a policy known as mercantilism, by which the Industry and Commerce, of the country were used as a means of securing National power, and the interests of the individual were subordinated to those of the country at large. (Penson).

This brought on many changes with it

- (1) Industry becomes diversified and there is a great advance in industrial art.
- (2) There was a good deal of improvement in the condition of labourer.

(3) In the towns the craftsman followed his own peculiar calling assisted by his apprentices and journey-men

*The Industrial revolution* This has been characterised by the following changes :—

(1) The introduction of machinery relieved the labourer of much of his manual work.

(2) There is an employer who owns the machinery and tools. Manufacturer no longer means the hand-worker, but the individual who employs others to work for him.

(3) Development of Capital led to keener competition. New classes of capitalistic middlemen arose

**Changes in Agriculture** (1) Crops were made much heavier and there was greater variety of them

(2) The cultivable area was increased.

(3) Large farming took the place of small and capitalism became a feature of agriculture just as it did of manufacturing industry.

(4) Agriculturer labour was put to much loss. He migrated to the towns where newly established industry created a demand for him.

(5) Men are now working in large industrial groups

---

## CHAPTER VI.

## E X C H A N G E

(1) **Total and marginal Utility.** In our study of exchange, we shall have to deal with certain terms which we must clearly understand. *Total utility* is the total satisfaction got by consuming a commodity. While *marginal utility* is the utility of a commodity which a person is on the margin of doubt to consume or not. If a hungry traveller sees an apple, it will have the highest utility for him. If he finds a second apple it will still be welcome but will satisfy a somewhat less intense want. With every additional apple his appetite will be more appeased, until with, let us say, the tenth apple, he will reach the point where he will be on the margin of doubt whether to consume any more. The utility of this tenth apple is called *final* or *marginal*, because on the margin of desire.

(2) **Barter.** It is an exchange of one commodity for another. In order to understand barter, we must study the conditions which are to be fulfilled before Barter can take place. A person has a certain thing and wishes to exchange it for some other thing which has greater utility for him. This implies that he has a desire to undergo a certain amount of sacrifice in order that he may get it. In a less complex society Barter takes place without any difficulty, but when there are more persons coming forward to transact business, exchange by barter becomes a difficult matter. In this case it would not be easy for a person to get the

best of the bargain in his transactions, and the range of final rates of exchange would consequently be reduced. This brings us to the difficulties of barter. It is true that when there are divisible commodities and when they have a proportional value, people will find it convenient to exchange them for other commodities. But where the commodity can not be divided without some loss of value, barter is of no use. Again, it is very difficult for a person to find out some one else who is in need of what this man possesses and can supply him the thing he wants. Money has been introduced to avoid these difficulties.

(3) **Value and Price.** "The word Value" says Adam Smith "has two different meanings and sometimes expresses the utility of some particular object and sometimes the power of purchasing other goods which the possession of that object conveys." The former is known as *value in use*, while the latter as *exchange value*. The exchange value of one thing in terms of another at any place or time is the amount of that second thing which can be got then and there in exchange for the first. Value expressed in terms of money is called *price*.

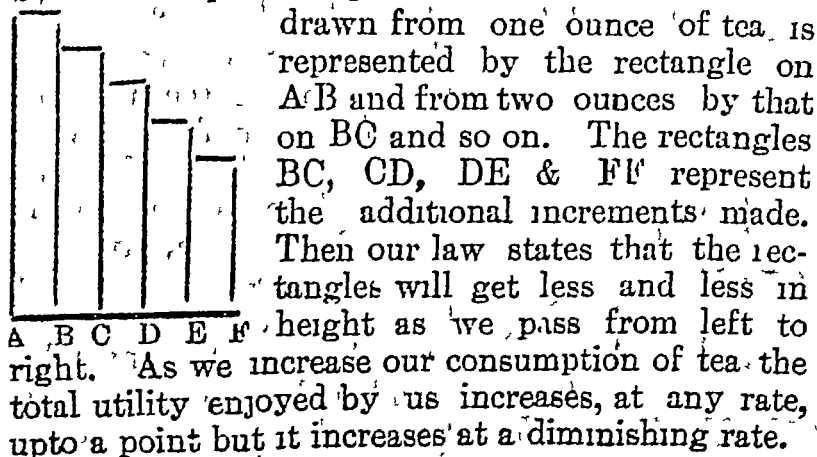
**How is Value determined ?** There are many considerations which a seller has in view when he offers any thing for sale. He tries his best to get a maximum price for his commodity, But he has a minimum also, beyond which he will not be willing to part with it. On the contrary, there is a buyer who has a certain maximum which he will be willing to offer if he thinks that

it would not be worth his while to purchase it at a higher price. Besides this he will try as far as possible to offer a little less than the maximum price. We, therefore, find out that the buyer has a demand for and the seller a supply of the commodities.

The price of commodities always fluctuates between the seller's minimum and the buyer's maximum. If the seller is not very keen about his minimum he will lower his price to a very small extent. On the other hand the buyer's demand being intense he will be prepared to push forward his maximum by a little bit. Thus a point will be reached when both the buyers and sellers will find it worth their while to settle the bargain. When there are more sellers and buyers the price is usually determined by competition. The sellers will sell their commodities to the person who offers the highest price.

(4) **Demand.** What really determines value is the interaction of the forces of demand and supply. Strictly speaking demand denotes desire. But there are other two constituents of demand. A mere desire to possess a thing will be of no avail if there are no means for purchasing it and also a willingness to forgo these means. An individual's demand for a commodity depends on the price of the commodity offered for sale. If the price be high, he will purchase less of it, if it be low, he will purchase more. But there is a limitation to this purchase put by a law known in Economics as the law of *diminishing utility*.

This law can be stated like this "With the increase in the amount of a thing a man has, the eagerness of his desire to obtain more diminishes." We become gradually indifferent to mangoes as we go on consuming a larger quantity of them until at last the utility, which we derive from them begins to diminish and results in disutility. Everybody is ready to purchase a certain amount of a commodity but after the point of satiety is reached his desire to obtain more decreases. If the price of that commodity had been a little less, he would have perhaps purchased more of it, but at the existing price he does not think worth his while to buy more of it. We will illustrate this by a diagram. Let AB, BC, CD, EF stand for successive increments of a commodity, say, ounces of tea consumed by certain persons per week. The satisfaction



**Demand Schedule.** It is a table showing the amount that would be demanded at each possible price. We will try to understand the schedule by an illustration. An umbrella manufacturer will

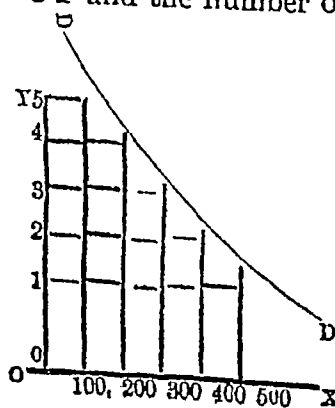
manufacture as many umbrellas as it would be likely for him to sell at the price he asks for them. If the price be less he will attract more customers, if it be high, he will find less people to purchase them.

If the price per umbrella, Annual demand will be

Rs	Re.	1	"	"	500
"	"	2	"	"	400
"	"	3	"	"	300
"	"	4	"	"	200
"	"	5	"	"	100

If these numbers are arranged in a diagram we will get the demand curve.

Let OX and OY be drawn, the one horizontally, the other vertically. Let units of price be marked on OY and the number of umbrellas demanded annu-



ally in a city be marked on OX. Now if the price be Rs 5/- per umbrella, very few people will come forward to buy them and the annual demand would be, say, 100. As the price is gradually lowered more people are tempted to buy and the annual demand tends to increase. If we want to know any intermediate prices for a corresponding number of umbrellas we shall mark the number on OX and draw a line vertically to this point intersecting the curve DD' which is called the de-

mand curve.

mand curve. From the point of intersection draw a line perpendicular to cut OX at a point. This point will be the price at which the given number of umbrellas will be demanded.

**Law of Demand.** We are now in a position to give a statement of the Law of demand. "The greater the amount to be sold, the smaller must be the price at which it is offered in order that it may find purchasers, or in other words, the amount demanded increases with a fall in price and diminishes with a rise in price." (Marshall.)

**Elasticity of Demand.** If a smaller alteration (rise or fall) in the price of a commodity produces a relatively larger alteration in the demand for it, then the demand is said to be *elastic*. Very few people buy watches in the ordinary circumstances. But if suddenly the price of these were reduced many people will come forward to buy. Thus a small fall in the price of watches has brought about a great alteration in the demand for them. Demand for necessaries remains nearly the same even if there is a great alteration in the price. If the price of wheat falls very much, people will not consume more of it than they do at present, while if it be very high they will probably consume as much as they do now. The change, if it be at all, in the degree of consumption would be very slight. This is the case of the inelasticity of demand. "If a considerable alteration in price fails to affect the demand much, then the demand is said to be inelastic."



(5) **Supply.** Supply is quite distinct from the stock which is the quantity of goods that could be sold, while the former is the quantity that could be sold at a certain price. The supply price is governed by the cost of producing the commodity offered for sale and the gain of the manufacturer therefrom.

*Elasticity of supply.* The higher the price, the more the sellers are willing to sell and vice versa. If the supply quickly responds to changes of price, it is said to be elastic, if it responds slowly or does not respond at all, it is said to be inelastic. Supply price is generally determined by short and long periods. If the supply is limited in stock and can not be increased at once it will be inelastic. But if time were allowed to multiply amount of the commodity demanded, it will be elastic. Different manufacturers have different cost prices. A profit to one may mean a loss to another. Then how are we to determine the price of a thing? This brings us to consider the *equilibrium of demand and supply*. When at any given time the demand is greater than supply, the sellers would ask more for their commodities. Thus more people will come forward to sell, and less will come to buy. On the other hand, if supply is greater than demand the sellers will lower the price. This will induce less people to sell and more to buy. Thus through changes in price, demand and supply gradually approach one another till they equate. The price at which they equate is called the normal or market price.

(6) **Markets.** In every day language the word market is used in more meanings than one. When we speak of a market our attention is generally concentrated on a building or enclosure where several kinds of provisions and other goods are offered for sale. But from an economic standpoint, this is not the real definition of markets. We may define the term Market for any commodity as a place or region where buyers and sellers are in free intercourse with one another. The buyers and sellers may all be in one place, as in the grain or cotton markets, but this is not a necessary condition, for people now can manage to live at a distance and still maintain free intercourse through posts and telegraphs. There are various stages in the development of markets the significance of which is well worthy of consideration.

(i) *Localization of markets.* It saves much of the time which used to be spent by buyers and sellers in moving about to meet one another. For a localized market, there is a certain place where goods are displayed. In such a place the buyers and sellers are crowded together and there is much competition between them. In the localized market there is likely to be one price at one time for one commodity.

(ii) *The system of selling by sample.* It saves the carriage of bulky goods to the market. In such Markets, there is a wider area of supply and competition within it grows more thorough-going in action.

(iii) *The adoption of selling by grade is a step*

*in the development of certain markets* For selling by grade the various qualities of commodities are arranged in separate classes to each of which is given a distinguishing mark or name. When grading has been effected, a buyer can purchase without seeing samples but by simply referring to the mark or name of the grade which he wants.

(iv) *Differentiation of markets* The original market is a mixed market. It is now split up into sections, into fruit market, the cattle market, the textile market and so on (Chapman)

(7) **Imports and Export of India.**  
**Imports.** We shall examine the salient features of import and export trade of India during 1922-23. Taking first import trade, we may notice that *cotton manufactures* are still the most prominent of individual items. During the year 1922-23, the total imports under this head increased in value to Rs 70 crores, as compared to Rs 16 crores in the pre war year 1913-14.

*Machinery and Mill Work.* This ranked next in importance to that of cotton manufactures. The total value of the imports of machinery of all kinds decreased from Rs 35 crores in 1921-22 to Rs 24 crores. The heaviest decreases were shown in jute mill machinery. Cotton machinery showed an increase in these imports.

*Iron and steel.* The third place in order of priority among imports was represented by iron and steel, which amounted to Rs 18 crores. The total imports under iron and steel increased in quantity from 613000 tons to 746000 tons.

*Sugar.* Trade was depressed, owing to excessive stocks held at the end of 1921-22, and heavy losses due to the continuous fall in prices of Java sugar. The total quantity imported both refined and unrefined decreased by 39 p c to 442000 tons. Generally speaking, the higher prices which ruled in the preceding years have given an impetus to the Indian sugar industry.

*Railway plant and Rolling Stock.* After the termination of war the value of imports under this head steadily increased from Rs 905 lakhs in 1919-21 and Rs 2,186 lakhs in the following year

The remaining articles of imports are Mineral Oils, Hardware, Silk, liquors and Motor vehicles. These showed a tendency to increase during the last two years

**Exports.** During the year 1922-23, *cotton*, raw and manufactured, displaced jute from the positions of priority. Exports of raw cotton from India increased to 3,362,000 bales as compared with 2,982,000 bales in 1921-22

*Jute.* Under jute and jute manufactures the figures of 1922-23 showed a marked improvement upon those of 1921-22. The total exports of jute cloth were 1254 million yards, valued at Rs 2,432 lakhs as compared with 1120 million yards valued at Rs 1,593 lakhs in 1921-22.

*Food Grains and Flour.* These amounted to Rs 4,249 lakhs in value as against Rs 2,999 lakhs in 1921-22. The total quantity exported amounted to 2.6 million tons, which represented an increase

of 57 p c. over year's figure due to the removal of *embargo* on the export of rice. The India wheat crop for 1921-22 was estimated at 9.8 million tons, as compared with 6.7 million tons in 1920-21.

The remaining exports are Oil-seeds, Tea and Hide and Skins. There was in fact a large increase in the value of exports of lac, jute manufactures, raw cotton, raw hides and skins, wheat, tea and linseed and rape seed while cotton yarn and rice showed some noticeable decrease. On the import side, the import under the category of food, drink and tobacco decreased by Rs 279 lakhs as compared with 1922 due mainly to smaller imports of wheat and salt.

---

## CHAPTER VII

### *MONEY AND BANKING.*

(1) **Functions of money** We saw (while standing the inconvenience of barter how money had to be introduced in order to facilitate exchange transactions.

The primary functions of money are three.—

- (a) To provide a general medium of exchange.
- (b) A common measure of value.
- (c) A standard for deferred payments.

(1) The seller of a commodity obtains money in exchange for it and with this money he can buy any thing he likes. Money effects the exchange only but this sort of exchange is quite different from the direct exchange by barter.

(ii) When we speak of money as a measure of value we refer to the values of the commodities at a given time. We measure the values of these things in terms of money and by doing so we compare the values of these things to one another.

(iii) In business transaction time is an important element. It is this time element which gives rise to the third function of money *viz.* to provide a standard for Deferred payments. Persons often make contracts to give and receive certain sums of money at future dates. These contracts are based on the value of money. The persons who make these contracts are certain about the stability of the value of money. If money means one thing in the beginning and something else at the end of a contract the expectations of these persons would not be fulfilled.

Closely allied to the above functions of money is its function as a store of value. When we save money, it is important that when we want it again we should be able to find it intact. It must not deteriorate by the lapse of time.

**(2) Qualities of a Good Metallic Money.** Historically almost every commodity has been used for money. Whatever happened to be common and widely wanted served as money. Articles of food like rice, wheat, etc. weapons like knives, implements, clothing made of wool or leather, animals such as sheep ; ornaments like beads, ivory, and metals like irons, copper etc. have been employed at one time or another. (Selgman).

With the spreading of civilization gold and silver came to be recognized as the best metals suited to the purpose. The characteristics of a good metallic money are as follows.—

(i) *Acceptibility*. In order that money should perform the function of a medium of exchange, it should be accepted by persons when it is offered in payment of any thing. People should have guarantee that what they accept they must, in turn, be able to pass on to others for exchange.

(ii) *Portability*. Because money is to be used for exchange transactions, it should be of such a bulk and weight as would be convenient for a person to send to some other place or to carry it himself from one place to another.

(iii) *Durability*. Persons do not make use of money as soon as they receive it. They wait until they are required to make other transactions with its aid. Thus the money commodity has to remain idle for some time. It should therefore be unamenable to deterioration and to the rapid wear and tear by use.

(iv) *Homogeneity and cognisability*. In order that money should perform the function of a measure of value, it should be homogeneous i.e. it should consist of such parts as are of an equal size and weight, and are of the same value. Besides this, people should be able to recognise it at once when it is offered for acceptance.

(v) *Divisibility*. This quality is closely allied to that of homogeneity. The money commodity

should be such as can be divided into parts without any loss in its value.

(vi) *Fixity of value.* As a standard for deferred payment the money commodity should always possess the same value in order that it may not occasion any inconvenience in being accepted.

(3) **Forms of Money.** In early times there were no coins; gold and silver passed in circulation in lumps. Payments were made by weight. This is known as currency by weight. Gradually these were given a definite shape and fineness. Shapes of all kinds were tried. But it was decided to have all coins made circular in shape with stamps on both the sides. With the advance of society, people began to realize the grave dangers of the coin being fraudulently counterfeited and some metal being removed from it. They then devised the device of milling the edges of the coins, which would soon detect these things.

(a) *Legal tender.* It is all money which can be offered in limited or unlimited quantities in full discharge of debts. All Government money is legal tender, and in England, Bank of England notes, except that they are compulsorily convertible at the Bank. In India the rupee is full legal tender. But in England no person is compelled to take in discharge of a debt more than 1s worth of copper coin and £2 worth of silver coins. The first coiners of money issued coins of one metal and of one kind only. This system is known as single legal tender system and the countries who adopt this are known as *Monometallists*. While those



countries in which two metals (gold and silver) are legal tender, are known as *Bimetallists*. *Standard money* is that which is legal tender for all debts and is used as the standard to which the value of other money is referable.

(b) *Token Coins* These are coins whose face value is greater than the intrinsic or metallic value, and whose coinage is not free in the sense that no person can demand that the Government should exchange his bullions for coins. These coins were issued to meet the demand of the people for small change. In India the rupee is a token coin, for its face value is greater than the value of bullion contained in it. For some years the coinage of rupee was free but in 1893 the mints were closed for free coinage.

**Coinage.** The term free coinage is employed in two senses. If the Government makes no charge for converting bullion into coin, the coinage may be said to be free. On the other hand, free coinage may mean the right of any owner of bullion to have it converted into coin. When we speak of free coinage of silver we employ the term in the second sense. (Chapman).

In England the Government has to coin the bullion when it is brought to the mint by any individual. It pays £3. 17s 10½d for an ounce of bullion. But the people there generally go to the Bank of England in order to save delay in time which the mint officers are generally liable to make. If the bullion is taken to the Bank of England, an ounce fetches £3. 17s 9d. People are ready to suffer

the loss of  $1\frac{1}{2}$ d than to wait for a week or so at the mint, for the Bank of England pays this immediately. There are some terms in this connection which need careful attention.

**Mintage or Brassage.** It is the sum levied to cover the actual costs of coming bullion. While *seigniorage* is the surplus charge representing a net gain to the Government

**Debasement.** When the seigniorage is imposed or increased on coins they are known as debased. In this case the standard value is greater than the value of bullion or the precious metal contained in the coin

**Value of Money.** *Depreciation* The value of money is its purchasing power and can be learnt only from the general level of prices. Prices of single commodities may rise or fall because of relative variations in the forces which effect particular demand and supply. But there can be no change in the prices of all commodities unless there is a corresponding change in the value of money. In order to understand the statement clearly, we will have to explain briefly the quantity theory of money. This theory is applicable to simple and primitive state of things. The theory states that the value of money (or the level of prices) varies *inversely* as its quantity, and *directly* with the number of commodities; if money is increased, prices rise, and if commodities are increased, prices will fall exactly in proportion to the increase. "We will illustrate this by an example. Suppose in a market there are only 100 commodities and 100 Rs. Also

suppose that all the commodities and all money are put into circulation. In this circumstance each commodity will cost 1 rupee. Now double the quantity of money. We find that 100 commodities are to be bought with Rs 200. That is to say more rupees have to do less work which means the purchasing power of rupee has fallen and prices have risen. Thus, an increase in the quantity of money has brought about a fall in the value (inversely). If, on the other hand, the quantity of money is kept unchanged and that of commodities is increased to 200, we shall find that less money will have to do more work. The result will be that for 1 rupee we shall have to purchase two commodities which means that the purchasing power of money has increased with a consequence that prices have fallen. There are other factors which determine the volume of money. They are rapidity of circulation, volume of exchange transactions and relations of credit to cash transactions. It is out of the province of the present treatise to deal with these factors. From the above illustration of the theory we have learnt that the purchasing power of money rises and falls. If the value or the purchasing power of money rises, we say that it has appreciated. On the other hand, if it falls, money is said to be depreciated.

**Gresham's Law.** Money the metallic value of which is equal to its face value is known as *good money*, while that money whose face value is greater than its metallic value is known as *bad money*. The briefest and most common form of statement of Gresham's Law is that '*bad money*' drives

out good money out of circulation but good money cannot drive out bad money out of circulation. Whenever there are two or more legal money in circulation, the bad or the light coins will displace good money which will be used as metal for export or for melting purposes. This law is not true in its entirety, for when there is a scarcity of currency in a country both good and bad money may circulate side by side even though one is of less value than the other. Gresham's Law is only a statement of tendency and as such it is true under certain hypothetical conditions. It may now be finally worded like this. When several forms of money are used in a country and if one of these is more useful for some other use than it is for making exchange, then the less valuable money will supplant the superior to the extent that the two portions together exceed the need for currency in country.

**Paper money.** Paper money is issued to economise the use of precious metals. Paper money may be representative in which case the cash reserve against the notes issued amount to 100 p.c. or it may be fiduciary or credit money in which case the part of the reserve may consist of securities. There are however several forms of paper money, but we will confine our attention to only two of them. The substitution of paper money for sovereigns results in a great economy in the costs of monetary system. Gold and Silver coins lose much of their value by wear and tear.

**Convertible Paper Money.** Convertible paper money is that which can be converted into bullion

at the option of the holder. The Government which issues such money always keeps in reserve a sufficient amount of bullion to meet the demands of the holders of notes "The Government in issuing these notes is really doing a banking business whose safety depends upon the degree in which the administration and the legislature understand the methods of banking." It is not necessary for the Government or the Bank issuing these notes to keep an amount of bullion equal to the actual notes in circulation. People, it is expected, do not generally demand bullion all at once. The amount of notes issued by the Bank of England is always  $18\frac{1}{2}$  millions more than the gold kept in reserve.

**Inconvertible Paper** All paper money for the redemption of which in bullion on demand no arrangements are made, is termed as "Inconvertible" or "Irredeemable" paper money. Only Government can issue such kind of money. It is not necessary that the inconvertible paper money should depreciate. If its quantity is stringently limited, it may circulate to its full value, particularly when people have faith in the issuer (Government) and in the ultimate convertibility of the notes. But the issue of such money is so profitable to Government, that no Government on earth has been able to resist the temptation to overissue it. In War times they are compelled to issue inconvertible paper to finance their heavy expenditure, and the paper money thus issued soon depreciates. When it depreciates, there is no limit to the amount of depreciation.

The two drawbacks of the overissue of paper money are .—

(i) The amount of money being increased, prices tend to rise (as we have seen while studying the depreciation of money).

(ii) "The other disadvantage of this money is that it cannot be used in international trade, because the merchants of other countries are not prepared to accept such money which is of no use to them and which they can not exchange for gold "

(4) **Credit.** Nearly all money whose metallic or intrinsic value is less than the face value is credit money, because its acceptance depends upon the credit of the Government or persons who put it into circulation. Credit depends upon trust and confidence. A person who accepts promissory note or a bill of exchange (to be explained later) trusts the person tendering it. Besides he himself offers it to others with a firm belief that it will be accepted by them. Credit facilitates transactions without the actual use of money. In a trade between persons living in the same country, credit finds no difficulty, but when we come to trade between one country and another, we must have some medium which should perform the function of money. When the currencies of the trading countries consist of the same metals, there is no difficulty in this. But still the metal is to be exported or imported as the case may be, to settle the amount of indebtedness.

**Foreign Exchange** The inconvenience and trouble of shipping gold is saved by what is known as *bills of exchange*. These are orders drawn by persons of the creditor country on those of the debtor country to pay up those amount stated in them. Importers who have to make remittances abroad purchase the orders issued by exporters of commodities to foreign countries, and send these to their creditors who realize the money from people on whom the bills are drawn and who are themselves saved the trouble of making remittances to their own creditors. If a balance of indebtedness remains after such adjustment has been made gold or silver is sent to make up the amount.

An illustration would make the above more clear. "A merchant A in France, let us say, has imported Coffee from M in Brazil, while B in France has exported the same value of silk to N in Brazil. Instead of A sending money to M and N sending it back to B it is far simpler for A and B to settle with each other in Paris, and M & N in Rio de Janeiro. B accordingly writes an order known as a bill of exchange to N directing him to pay M, or in technical language B draws on N; A buys this bill from B and remits it to M who presents it to N and gets it cashed. Thus no money is exported but only one bill is drawn. In as much as it is not always easy for the M's and N's to find each other in Rio de Janeiro, and the A's and B's in Paris, the business of issuing and purchasing such bills has become the function of the banker and the brokers" (Seligman).

We will summarise the above in the form of a table.

France

Brazil.

A	B		M	N
Importer of coffee	Exporter of silk		Exporter of coffee	Importer of silk
A buys the draft and remits it to M	B draws on N		M presents it to N	N pays it

Bills of exchange serve the following purposes:—

(i) They give the owner the right to receive a specified sum of money at a given place and time, and this right can be bought and sold.

(ii) They provide a cheap and convenient way of paying debts incurred in a foreign country.

(iii) They enable a merchant to be paid for goods sent abroad in the money of his own country.

**Indian Currency** We will try to give very brief summary of the Indian currency system and its development

There were several kinds of coins in circulation in India during the ancient times. Each kingdom possessed its own coins. Gold and silver coins were in circulation, but there was no fixed rate between them.



The confusion caused by the multiplicity and variety of coins led the East India Company to think of making the currency uniform. In 1806 the Directors of this Company directed that the coinage should be uniform. Though silver rupee was the principal measure of value, yet they "did not wish to introduce a silver currency to the exclusion of gold. It was in 1818 that the silver rupee was substituted for the gold pagoda of Madras presidency."

In 1835 the present silver rupee was formally established as the standard coin of the whole of British India and gold was demonetised. It was enacted that "no gold coin shall henceforth be a legal tender of payment in any of the territories of the East India Company." But in 1841 the officers in charge of public treasuries were authorised to receive gold Mohors at fixed rates which represented a ratio of 15 to 1 between silver and gold. But the excessive discoveries of gold in Australia diminished its value and the order was withdrawn. In 1864 sovereigns and half sovereigns were made legal tender at the rate of one sovereign for 10 rupees.

In the year 1873 the value of silver relatively to gold began to fall because the world's output of silver was much increased. This was due to the adoption by the countries known as Latin-Union (France, Belgium, Switzerland and Italy) of gold as legal tender and the suspension of the free coinage of silver. Thus silver flowed to India and the gold value of a rupee fell continuously. The

Government of India suggested the adoption of gold standard while retaining the silver currency but the proposal was vetoed by the Imperial Government.

**Currency Committes.** There were nearly four committes which sat from time to time to consider the currency problems of India. We shall attempt a very brief survey of the work done by them.

*Harshell Committee.* When the value of silver began to fall and the Government could not succeed in having a gold standard, the Secretary of the State for India appointed a committee to inquire and report on the matter. "In accordance with the recommendations of this Committee, Act No. VIII of 1893 was passed providing for the closing of the Indian mints to the free coinage of both gold and silver, reserving the power to Government to coin rupees on its own account. Gold was received at the Indian mints in exchange for rupees at the rate of 16d per rupee." But in spite of this act the rate of exchange rose temporarily, but could not be maintained and fell further even than before till in 1894.5 the average rate was 13.1d. per rupee.

*Fowler Committee* This committee was appointed in 1898. The committee declared itself in favour of the effective establishment of a gold standard accompanied by a gold currency. The rupee was to continue as legal tender upto an unlimited extent. The value of rupee in terms of gold was fixed at 1s. 4d. The profit of the coinage of

rupees was to be kept in gold as a special reserve entirely apart from the paper currency reserve and the ordinary treasury balances. These proposals were first accepted but soon afterwards the Government began to drift from them. The proposals were neglected and India came to have a gold exchange standard instead of a pure gold standard.

**Gold Exchange Standard** Gold is not used by people for ordinary transactions. The bulk of metallic currency consists of coin which circulated at an artificial value far greater than the intrinsic value. The government makes this currency exchangeable in the international money market. Since 1898 the value of rupee has not fluctuated to any important extent except for a brief period during the crisis of 1907-08.

**Gold Standard Reserve.** This was proposed by the Fowler Committee and was to be formed out of the profit on the coinage of rupees. The gold thus accumulated was to be made available for foreign remittances whenever the exchange fell below gold or specie points (points at which it was more profitable to remit bullion by shipping it). Up to 1906 the whole amount was remitted in England but in that year it was decided that a portion of the reserve should be held in India. In 1907-08 it was further decided to divert half of the profits on coinage to capital expenditure on railway.

Before we proceed to the report of the Chamberlain commission we shall briefly consider India's method of making foreign remittances. In India

the standard of value has been for many years a silver rupee. If there was a fall in the value of silver the Indian exporters were benefited by it, because they got more rupees for less sovereigns. But the Indian importers were at a loss for they had to pay more rupees to get the same quantity of sovereigns in London. With the adoption of Gold standard the problem of exchange became easy and fluctuations in the rate of exchange were limited. Secondly the Secretary of State has to spend large amounts of money in London on behalf of India. He realises these amounts by selling council bills on the Indian treasury. These bills are paid by the Indian Government in India. The European importers of Indian goods, who want to send money to India buy these bills and send them to the Indian Exporters (their creditors) who get them cashed at the treasuries.

**Rate of Exchange** The rate of exchange is the rate at which a definite amount of foreign money can be obtained in that foreign country by payment of money of one's own country. Mint par of exchange is obtained by establishing a comparison between the currencies of the countries concerned based on the weight and fineness of precious metal contained in their respective standard coins. The actual rate will be above or below it if a country has to receive more or less from foreign countries than it owes to them.

Fluctuations in the rate are limited to gold or the specie importing or exporting points, that is, the limit at which bullion or specie will be imported if the balance of trade is adverse or favourable.

The Indian exchange is expressed by stating that one rupee will buy 1s 4d. in London, while a sovereign will buy Rs 14-15 as in Bombay. As we have just seen, the Government by selling reverse councils and by accepting council bills maintains the value of rupee from being lowered. The rate of exchange in India will rise when there is a great demand for remittance to pay for Indian exports and will fall when exports are reduced and when there are very small payments to be made to India. When latter is the case, i.e. when the balance of trade is unfavourable to India, the method of council bills fails, and as there is a great demand for exporting gold, the Government of India has to sell sterling bills on London which are known as reverse councils. These are met in London from the funds in the gold standard reserve.

*Chamberlain commission* Recommendations of this commission were as follows —

- ✓(i) Use of notes should be encouraged.
- ✓(ii) The Indian branch of paper-currency should be abolished, the rupees being handed over to the paper currency reserve in exchange for gold.
- ✓(iii) The invested portion of the paper currency reserve should be raised from 14 to 20 crores.

The Government could not deal entirely with the report owing to the sudden outbreak of the war

**War and Currency.** The gold exchange system broke down during the war. The rise in the price of silver destroyed it. It has been proved once more that the gold exchange system guarantees a stable exchange, provided the price of silver remains steady. The price of silver began to rise in 1916 and in May 1917 it rose to 57 d much above the bullion par of the rupee. The rupee began to be melted and special legislation had to be enacted in order to save it from being so. The rise in exchange proved very welcome to the Government of India, as it reduced the burden of their sterling obligations.

**Babington Smith Committee.** In 1919 a committee was appointed under the chairmanship of H. Babington Smith. On the recommendations of this Committee the official money standard was changed from 15 Rs. to the sovereign to 10 rupees to sovereign. The rupee was then made equal to two shillings in gold. Owing to several difficulties the Government failed to maintain the rate and ultimately it let the exchange have its own course.

**Paper Money.** Before 1861 several private bank notes were issued, but in that year the Government withdrew the privilege of issuing notes from the presidency Banks, and undertook the issue of paper money itself, so that it may be secured by adequate reserve and be made legal tender. In 1862 India was divided into circles of issue, there being a currency office in each circle. After 1910 notes of the denominations of 5, 10, 50 and 100 were universalized. In 1917 one rupee notes were

issued followed by notes of Rs 2/8 which are now abolished

**Paper Currency reserve.** By the original act of 1861 the paper currency was established. The reserve may be held up to the amount of 120 crores in the shape of investments either in England or in India of a kind which bear interest.

In 1920 an Act was passed abolishing the limit on the holding of securities of the Government of India

**Banking. Development** In England the banking system originated from the goldsmiths. People found it unsafe to keep large amount of money with them, so they deposited this money with the goldsmiths. But these goldsmiths afterwards found out that they could conveniently lend some money out of the deposits and yet meet the demands of the depositors. They then began to lend money on a small interest. There arose gradually small bankers who took deposits and allowed interest upon them. The banker learnt in due course of time that as his credit increased, he might issue his own promise to pay, in the shape of Bank notes. The first bank of issue was the Bank of Amsterdam founded in 1656. The bank of England which is the earliest important bank was founded in 1694. It is with this Bank that the modern banking may be said to begin.

**Functions** The two primary functions of a bank are deposit—receiving money and discount—lending it on a certain interest, a third function is

also attributed to the Banks viz. of issuing notes. But this function belongs to the central Banks in other countries. In India the Banks do not issue notes. The various functions are the following:—

(i) They remit money from one place to another on behalf of their clients.

(ii) They act as Agents in buying or selling securities

(iii) They finance a country's trade and industry.

Where no banks exist, people generally keep money in hoards. This does not come into circulation and hence lies useless. But the bank by affording security brings this money into circulation and thus helps the trade and industries of a country. With these preliminary and general remarks on banking we shall now turn to the Indian Banking system

**The Indian Banking System.** The Indian Banking system consists of the following :—

(i) The Imperial Bank (formerly the Presidency Bank)

(ii) The exchange Banks doing business in this country as well as others

(iii) The Indian joint stock Banks.

(iv) Indegenous banking houses and bankers viz. Shroffs, Mahajan.

The Presidency Bank occupies a unique position in the Indian banking system. The Government was a share holder of the bank and it (Government) has always deposited large sums



with it. With the growth of more banking business, people found it necessary to have one central Bank. As the interest of all the three Presidency banks were the same, it was urged to amalgamate them into one. By the act of 1920 the Imperial bank was constituted. The capital was increased. The authorised capital of the new bank was fixed at Rs 1125 lakhs. The Governing body of the new bank was a central Board. There were the President, and Vice-presidents, the Controller of the Currency, Secretaries and one or two Managers. The functions of the Bank are :—

(i) Advancing and lending money.  
 (ii) The drawing, accepting, discounting, buying and selling of bills of exchange and other negotiable securities payable in India or Ceylon.

(iii) Receiving of deposits and keeping cash accounts. The Bank has an office in London. By agreement the Government have appointed the Bank as their sole bankers in India.

**Exchange Bank** These banks finance foreign commerce. They receive deposits in India and seek to attract these in order to obtain funds required for the purchase of discount of export bills or exchange. They have got their head offices outside India.

**The Joint Stock Banks** These banks are of a recent origin. The early joint stock Banks were all under European management. But during the last 15 years a number of important Joint stock banks have been established under Indian Board of Directors and their share capital was

entirely supported by Indians. "In 1913 and 1914 about fifty of the newly started banking concerns had to be closed. The bank failures entailed loss and misery upon thousands, but they taught a lesson in banking management".

**Indigenous Banking.** The shroffs live in all towns and they finance nearly the whole of the internal trade of India, but they never purchase foreign bills. The bulk of their business consists in discounting trader's Hundis, and in making advances. In the village the Mahajan lends money to the agriculturists at an exorbitant rate, loans are taken by the people on the security of land notes, or *pawns* of jewellery or as some times is the case, by mortgage of property. Co-operative credit societies are doing good work to help people in this respect. We shall have to consider these societies fully when we come to distribution

---

## CHAPTER VIII

### *DISTRIBUTION.*

**The Problem of Distribution** The economics of distribution accounts for the sharing of wealth produced by a community among the agents or the owners of the agents which have been active in its production. The aggregate of the income of the people working in an industrial group is known as joint income. It is this income which is to be distributed among the members of that group. But when we say that this income

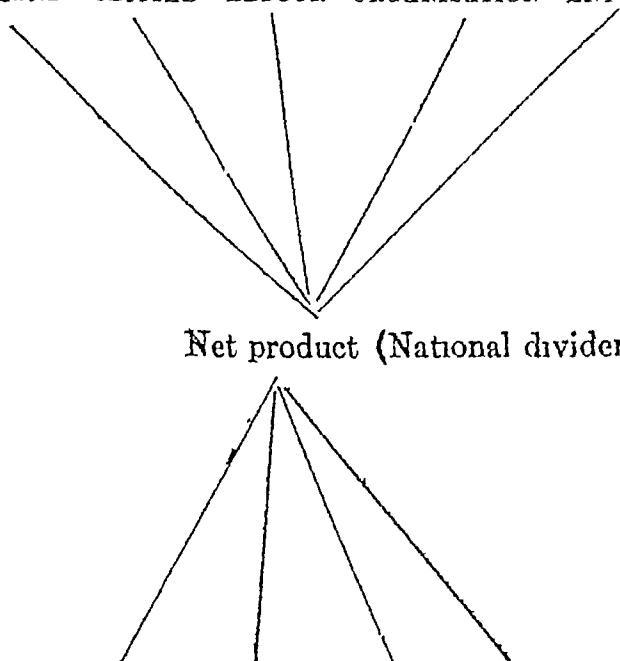
is to be distributed, we are naturally led to ask "what should be the share of each individual in that group?" Of course a person will be paid in proportion to his services. But it is at times difficult to measure the services rendered by such persons. For, in such a group each person has not completed any work but has partially helped towards its completion. Cases there are where the question of distribution does not arise at all. Suppose there is a farmer owning a land. This farmer farms it without any aid of labour and consequently the output which the farm yields will go to him alone. But such cases are very rare. In India it was true upto a certain time. But now-a-days the agriculturist is required to depend upon others for the capital which is required in production. In most case the cultivator himself is the labourer.

With the advance of industrial life, there arose classes of employers and the employees. With them the problem of distribution became still more difficult. It is said that there is an antithesis between the two classes regarding the share of each in the distribution of the wealth that is produced by them. But so far as the production of wealth is concerned, the interests of the two parties are harmonious and the antithesis is unreal and misleading. But when we come to the distribution of this produced wealth, the antithesis becomes real. For the larger the share of one party, smaller must inevitably be the share of other. The problem is of great importance, but it would be out the scope of an elementary treatise as this to dilate upon it any further.

We now come to a second question regarding distribution *viz.* "what is distributed"? That which is the result of the joint effort of the agents of production is said to be distributed. But before we divide this income among the agents we have to take notice of the difference between the total out-put or gross product and the net product. The *Gross product* is the whole output of the industrial group. From this gross product some income is laid aside for the replacement of the *fixed* and *circulating* capital of a business undertaking. Buildings, machines, tools etc do not last for ever, but wear out gradually and a time comes when they have to be replaced. If a producer does not provide for their replacement out of his produce but distributes all of it under other heads, a time must come when his production is brought to a standstill. Hence the income which the producer sets aside for this 'depreciation of capital' is to be deducted from the gross product. The remaining is known as the net product. This net product of an industry is what is distributed among the factors who helped to the production of the total output. Persons who have contributed to the production of a thing are entitled to receive a share of the Net product. Services are rendered only when people expect to get something in return for them. There are hence as many shares in distribution as there are factors in production. The remuneration of labour is called wages, that of capital interest, that of land rent, that of the organiser salaries and that of the *entrepreneur* (the man who provides enterprise) profits. For

convenience sake, let us arrange the above in a tabular form,

LAND CAPITAL LABOUR ORGANISATION ENTERPRISE



Net product (National dividend)

Rent Interest Wages Salaries Profits

When we add all the net products of the industries carried on in a country we get the National Dividend.

**Method of Distribution** The real distributor, we may say, is the person who undertakes productive enterprise. He hires the land, labour and capital which are required in addition to any which he may himself provide. He calculates what the product of a particular business undertaking would be and then makes contracts with the other agents

he has hired, to pay them leaving a sufficient margin for his profits in the undertaking. If the business is a failure, the organiser will be at loss; for he is bound by contracts to pay the other agents their due. But if it be a success, the excess of the profits goes to him.

When the organiser hires other agents, he has to take into consideration the supply and demand of these factors. The remuneration which will be finally paid to them will depend upon the interaction of these two factors of demand and supply. Take for instance the case of labourers. These will have a certain minimum (price for their services) at which they are willing to work, on the other hand, the organiser will have a maximum price to offer beyond which he will not think it worth his while to proceed. After much (bargaining) hesitation on both the sides, the normal wages will be settled under which both the labourers and the organiser will come to an agreement. We will now consider the shares of the each of the factors separately. We first take up *rent*.

**Rent.** The term rent has got a very wide meaning in common parlance. We speak of the rent of a building furniture, lands etc. When we use the term in this sense, we mean by it the amount which is paid to the owner of the things for a limited or periodical use of those things. But in economics the term has got a very restricted meaning. It is usually associated with land, mines, water power etc. Suppose a farmer cultivates his own land. In this case the economic

rent will take the from of the excess over and above the cost of production and the gain of the farmer. Among the classical writers on economics, Ricardo's theory of rent is the one which has been handed down to us. He defines rent as that portion of the produce of the earth which is paid to landlord for "the original and indestructible powers of the soil." It is true that these powers are not found in each and every land. Men's efforts have proved successful in changing the condition of the soil altogether and even the least fertile lands have been made to yield a tolerably good produce. But although improvements in this direction have gone far, there remains a certain kind of difference in the degree of fertility between lands which are under cultivation. Ricardo based his theory on this difference in the degree of fertility. He made clear one of the fundamental assumptions that the same amount of labour and capital or productive power is applied under different natural conditions, but not necessarily to the same amount of land. In summing up his theory of rent we may say that he regarded rent "as the differential profit that arises from differences in the costs of production, owing to differences in permanent natural conditions."

**Kinds of Rent.** With this preliminary introduction, we will now find out how many kinds of rent there are. In the case of a farmer who owns a land and cultivates it himself, we have seen that the rent was the excess over the cost of production and the farmer's gain. If he does not cultivate the land himself, but lets it out on hire

to a tenant he will get what is called contract rent. We should bear in mind that we are at present considering rent of agricultural lands. We can now divide this rent into (1) Economic rent and (2) Contract rent. When we come to the consideration of other rents besides this, we will see that they arise owing to nearly the same causes. We will then deal briefly with ground rents and rents of mines, fisheries etc.

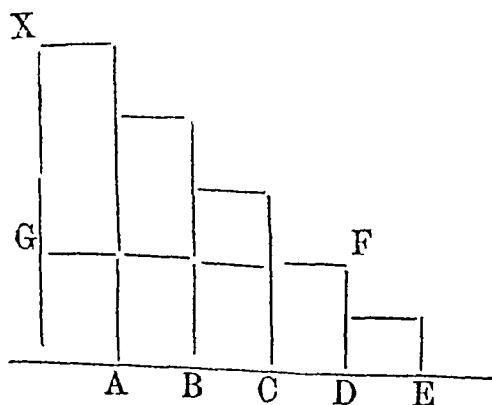
**Economic Rent.** We saw just now that the lands which are under cultivation do not possess the same degree of fertility. Under such conditions it is easy for us to find out how the economic rent emerges. A land which is cultivated but bears no rent is called the 'land on the margin of cultivation'. This means that it just pays the cultivator to farm it, and if there were some slight changes in the conditions of supply and demand he will give up the cultivation of such lands. We will now illustrate how economic rent emerges. Let us take for granted that there are various kinds of lands and that their quantities are limited. As population increases the yield from the best land will not be sufficient to meet the demands of the people. Thus prices will rise. And at such high prices it will be profitable to resort to lands of inferior quality. This means that the margin of cultivation will be pushed forward. The land which was on the margin of cultivation at first has now begun to yield some rent. Under such conditions the rent will be determined in the following manner. Although there is a rise in prices of agricultural produce yet it is true that the



amount produced will be sold at the same price. Thus differential profit will emerge from the best lands. This profit then constitutes economic rent. If on the other hand, the prices of agricultural produce fall, it will not be worth while to cultivate the land on the margin of cultivation. Thus the differential profits will be reduced as a consequence of which rent will decrease. We are now in a position to give the final statement regarding economic rent as given by Moreland. "Whatever the prices of produce may be, some of the land under cultivation will only just remunerate the labour, capital and management employed on it, this marginal land will pay no rent, while all the more productive land will pay as rent the entire surplus of its production that is left after remunerating the other factors employed on it. This surplus then is known as economic rent."

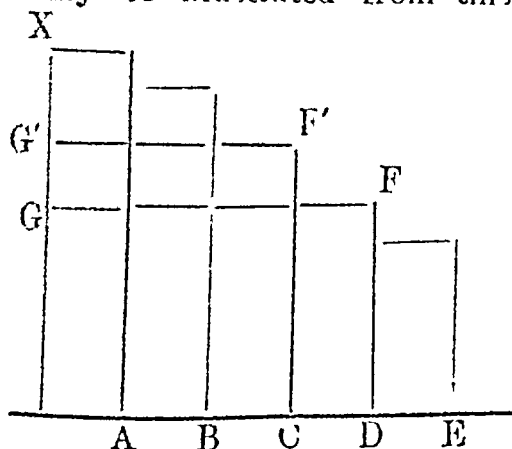
We will attempt a diagrammatic treatment of economic rent

Let A, B, C, D and E be lands of different qua-



lities. Let D be the land on the margin of cultivation. That is to say it just pays to bring the land under cultivation. It is to be known that the cost of production is the same on all grades

of lands. As the D quality of land just pays the cost of production and as it does not pay any rent, being on the margin, we will take D F to be the actual cost of production including the gain of the farmer. The economic rent then will be the figure XGF. We see that this rent varies with the lands of other qualities. With the A' quality it is the greatest and while with the C quality it is the least. The rise and fall in the amount may be illustrated from this very diagram. If



suppose price fall, the margin of cultivation will recede to C which now will be the land on the margin of cultivation. This means that the cost of production has increased, in our diagram

C F' now measures the cost of production. In this case the economic rent will be X, G, F', which is obviously less than XGF. Similarly it can be shown that rent increases with pushing the margin forward.

**Contract Rent** When a landlord lets his land to a tenant, he makes an agreement with the latter to pay him a certain amount for his enjoying certain advantages either of fertility, or of situation. This payment is known as contract rent. It depends upon the interaction of the forces of demand and supply. Demand arises from the

tenant, while supply from the landlord. The tenant will offer as much for a particular piece of land as will enable him to pay the contract rent after deducting the cost of production and his gain therefrom. He will be ready to offer a maximum price for the land. Above this price it will not be worth his while to take the land for cultivation. This maximum price depends upon the character of the soil and the situation of the land. If the land were very fertile, tenants would rather increase their maximum. Thus the greater the advantages derived from the land, the greater will be the quantity demanded and *vice versa*. Coming to the side of supply, we find that the landlord has got lands which he can utilise for different purposes. He can cultivate some of them himself or let them to tenants. The supply will no doubt depend upon the price of the land which he can get for it. If the rent (price) is very low, he will consider worth his while to cultivate it himself rather than let it out on hire. If there is a scarcity of lands in a country, the demand for land will rise which means gain to the landlord, for he can then get as much rent as he wishes. On the contrary if the demand falls, the rent will tend to lower until it will be equal to the minimum price which the landlord is willing to take.

**Rent does not enter into the cost of production.** It is said that "prices are high because rent is paid." But it is not true. On the contrary, it may be said that rent is paid because prices are high. Rent depends upon prices and not prices on rent. When prices are high, people

take up farming inferior qualities of lands which means that they are willing to offer more for these lands. The increase in the offer of the tenant is really an increase in the rent received by the landlord. On the other hand, when prices are low, farming becomes less profitable, this means that the tenants offer less for lands (demand falls) and the rents received by the landlord tend to decrease.

**Ground rent** This is of two kinds viz: Economic rent and contract rent. If the landlord builds a house on his own land he may be said to derive an economic rent from its use in as much as he enjoys all the advantages which are obtained from that land. But if he lets the land to a builder for a certain period (usually 99 years) the latter has to pay a certain annual sum or contract rent to the land lord. The amount of this rent is fixed by bargaining between the two parties.

**Law of rent as applied to India.** Rent in India depends on the interaction of three forces, Custom, Competition and Legislation. In ancient days custom was the chief regulator of rents. With the increase of population and the gradual disappearance of semisocialistic ideas which used to govern the mutual relations of the ancient village communities rents began more and more to be regulated by competition. This led to great hardships. Landlords began to exact excessive rents from their tenant. The Government was required to intervene and rent laws were passed. The theory

of rent which we have just explained is not applicable to India. Here rent does not necessarily represent the difference between the produce of any particular plot and the plot on the margin of cultivation. Rent is more or less a definite charge. Productivity is, no doubt, a factor in the determination of the actual rent of any plot but it is only one of several factors. Rent is often an element in the cost of produce (Banerjee). The land here has been occupied and it can not be had freely. Therefore the price of land (or its rent) is determined by competition. The Government has led down legislative measures to protect the tenants from the undue exactions of landlords, who can increase the rent payable to it by tenants.

### Land Tenures in the United Province.

It was only in Benares that settlement of land revenue was made permanent. In 1882 the court of Directors declared themselves against it and in the same year fixed the state demand at 83 p c. of the gross rent earned by the states. This system became tedious afterwards and in 1883 during the Government of Lord Bentinck, the first regular settlement on broad principles of action was made. This settlement was made with the village proprietors and zamindars on the principle of joint responsibility. Hereditary tenants and tenants who have occupied the land for twelve continuous years were given the rights of occupancy. The assessment was reduced to 66 p c. of the rental and a settlement for a term of 30 years was introduced. This rule was also changed and the Sherampur rule of 1855

reduced the land tax to 50 p c of the average produce

Tenancy laws are enacted to protect the tenants against the effects of unfair competition and to secure him the rights conferred by custom. A tenure holder is a person who has acquired from the proprietor or from other tenure holder a right to hold land for the purposes of collecting rents or bringing it under cultivation by establishing tenants on it. In the permanently settled districts of the Agra province there are certain tenants holding tenures at fixed rates. Other tenants if they hold for twelve years, become occupancy tenants. Tenants of less standing are tenants *at will*. Ex-proprietory tenants are those who are in possession of land as occupancy and who were in possession of the same land as proprietors, these tenants have a privilege of reduced rent which is usually 25 p c below that of ordinary tenants

**Wages.** Workers who contribute towards the production of an industrial group differ from one another in some respects. Some workers do exclusive mental work as is required in the management of the business, while other render purely manual labour. It is therefore, expedient to divide these workers into classes which will vary according to the quality of the services rendered. Firstly there is the business organiser. His income consists of the salaries he receives if he is under a joint stock company. This company is formed on the joint responsibilities of the shareholders. The management is under a Board of Directors, the

Managers or Supervisors are paid servants. Thus a business organiser is a servant of such Company and his salary will depend upon the interaction of the forces of demand and supply. There will be a demand for his services at a certain amount of salary which the company is willing to offer and the supply will depend upon the number of such technically trained persons available at the time. In a private business undertaking the organiser's income is not like a definite salary. It will depend upon the net product or the annual output of his business concern. He will only have a share out of it, after it has been distributed among the other agents of production.

In the 2nd place there are highly paid officers such as manager, clerks, etc. There are certain posts in a business concern where only men of a very high degree of skill and knowledge are wanted while there are such positions where an ordinary educated person will do. The market for such persons ('supply') is more extensive because there is a greater mobility among these classes than is the case with ordinary labourers. Employers will look for men with particular qualifications not in one town, but all over the country and even 'outside its limits'. But the supply of persons having skilled training and a higher degree of knowledge is restricted. With the spread of general education in India many persons are entering such employments. Whenever there is any vacancy in any of these employments, we find that hundreds of applications are received from the candidates.

There is a third class of labourers known as the skilled labourers. Formerly the wages of such labourers were very low. They just supplied the labourers with the bare necessities of life. The chief reason was that there was a rapid increase in the population which led to an unrestrained competition among such skilled labourers. As a consequence, the wages fell much below the normal wage. To remedy this the movement of the *trade unions* was started. "This is a continuous association of wage earners for the purpose of maintaining or improving the conditions of their employment" (WEBB. History of Trade Unionism). These have succeeded in putting an artificial restriction over the supply of labour which consequently raises the wages. Now-a-days the skilled labour is very well organised and the wage contract is settled by collective bargaining between the Association of the employers and the trade union officials.

Finally we come to the fourth class *viz* unskilled labourers. The trade unions have been formed in very few of the employments which require the services of the unskilled labourers. The work required in these businesses is of such a type as any person with an average strength and intelligence can do. Consequently there are many persons coming forward for such work. An increased supply tends to lower the wages which they receive. We now pass on to the consideration of those forces which determine the rate of wages that are paid in return for services rendered. The amount of wages depends upon the conditions of demand and supply. The demand consists of



the employers who want men for work, and the supply consists of the labourers who are ready to work.

**Demand for Labour.** Demand for labour arises because there is a certain amount of work to be done in return for the payments of wages. This demand is not a fixed quantity. It varies with the amount of wages very much in the same way as the demand for commodities varies with the price. If the workers ask more than what the employer is willing to pay there will practically be no demand and the employer will refuse to engage the labourers. He has his maximum above which he will not think worth his while to go. This maximum will be determined by the amount of wealth the labourer produces.

“A person will not pay a coolie two annas to cut grass if the grass is not worth two annas to him, he will pay less than the grass is worth to him if he can get the coolie to work for less but he will not pay more” (Moreland). Similar is the case with an organised industry. The employer will continue to employ more men as long as he thinks that the output produced by the increased number leaves behind sufficient profits. When his attention is thus directed to the gain he obtains, he will employ the last man who in his opinion just remunerates him for the wages he pays. This last labourer is known as the *marginal labourer* because the employer is on the margin of doubt to employ him or not. Increase in the number of labourers is profitable upto a certain extent, but after that any additional in-

crease will mean a loss to the employer. We saw when studying production on a large scale that the division of labour is limited by the extent of market. This means that a business concern should produce as much only as is in its opinion likely to find suitable market. If the storehouses are filled up with the goods produced and if these goods cannot find market there is no use of producing them at all. It is, therefore, that employer should produce as much as will find a good market, and for this only a certain number of labourers will be sufficient. From the employer's point of view the changes in the rate of wages are of great importance. If the rate rises he will be inclined to reduce the number of labourers on the other hand, a fall in the rate will induce him to employ more men and get his work done within a short time. We can then represent the demand for labour on the lines of the general law of demand that a rise in wages will reduce the demand and a fall in wages will increase it. There is a last factor in the demand for a labour viz. efficiency of the labourers. The amount of produce raised varies with the qualities of labour applied. 'This fact is well known to employers. Contractors for instance, know that they can pay higher wages for earth work to labourers from Oudh than to the labourers from Central India, because the former do more and better work than the latter' (Moreland).

**Supply of Labour.**—The supply of labour is restricted by the number of persons who are able and willing to do certain kinds of work. If it requires some skill in the performance of such

work, there will be a less number of people offering themselves to do it. If, on the contrary, the work is quite an ordinary one, nearly all persons of an average strength will be able to do it. If the labourers find that a particular branch of industry is more profitable they will try to enter into that industry and learn as apprentices the manner in which work is to be done. A long time will be required to make them efficient workers in that branch. The supply in this case will be increased after a long time. The supply consists of labourers who are able and willing to do certain kind of work at a rate which will enable them to obtain the bare necessities of life. (An increase in the rate of wages means that the labourers will be able to get larger amount of commodities needed for consumption.) Consequently the supply of labour will be increased. Labourers are really attracted not by the money wages but with what the money will buy. The expression *money wages* means the amount of money which a labourer gets as a remuneration for his services. While *Real wages* include the quantity of commodities, such as food, clothing etc that can be obtained by means of that money. The *Real wages* depend upon the prices of commodities. If the prices rise the money wages remaining the same, the labourer will get a less amount of commodities. This will make him leave the occupation at once. If prices fall, the money wages will enable the labourer to buy a greater quantity of commodities, and as a consequence of this his condition would much improve.

The trade unions have given the workers a certain minimum or reserve price for their services. If the wages fell below this minimum, no labourer will come forward to work under which conditions, the employers will have to raise wages. This minimum keeps a certain standard of living among the labourers. The way of life to which labourers of any grade are accustomed is usually spoken of as their '*standard of life or comfort*'. This standard varies from time to time and place to place. In some parts of India, the labourers get nourishing food, good clothes and shelter. Besides, they can spend small amount of money on petty amusements. While in other parts the labourers are paid low wages. This lowers their standard of living. If bad times come when there is little work to be had and labourers are not able to earn as much as usual, they cannot of course maintain their standard of comfort: they must eat less, and have to put up with inferior food, and they must wear less clothings, but when the conditions of employment improve, they (labourers) return as soon as possible to their old standard (Moreland).

We have been up till now considering the effects of the factors of demand and supply on wages. Let us now see how they determine the normal wages or bring about an equilibrium in the rate of wages. If demand is great i.e. if the labourers demand higher wages than the employer is willing to offer there will be no settlement at all. No labourer will be employed. If on the other hand the employer just raises his maximum (price

which he is ready to pay) many labourers will be induced to offer themselves for work. The actual rate will be settled after such bargaining on both the sides.

**Mobility of Labour in India.** Mobility of labour is the degree of facility with which in response to any inducement labourers move from one place or employment to another. In India the labourers are not evenly distributed. There are cities which are overcrowded with them, while there are some towns or villages which can still accommodate a good number of labourers. Secondly, mobility in India is a question of caste and locality. There are persons of some caste who will be found nearly everywhere in India. "Thus Chamars from Jaunpur and Azamgarh are found working as grooms in almost every town, Brahmins and Chattris of Oudh go to the more distant parts to work as sepoy and peon." (Moreland)

But India chiefly being an agricultural country, the people who follow this pursuit as well as the field-labourers scarcely move from one place to another. Quite contrary is the case with the artisans. They move much more easily to places where they hope to get profitable employment, because they are in a position to carry with themselves their tools and implements. The Agriculturist, on the other hand, cannot do so. He has lived in a particular place for many years and has studied the peculiarities and nature of the soils of his fields. He has also understood the climate conditions and the raising of crops at each harvest. If he is made to shift from his old residence, he will have to

encounter many difficulties which present themselves in the form of new and strange soils, climate condition and crops. It is therefore particularly true of the Indian agriculturist that he is very slow to move. Besides the agriculturist there is the factory labour. It is only recently that the Indian factories have begun to attract labour from rural areas. The labourers have now come to understand that they are better off in factories and mills than they are on the fields. There is one point to be noted here in this connection. The factories are affording many facilities to these labourers building quarters for their shelter and paying them tolerably good wages.

Apart from the mobility from place to place, there is the mobility from one employment to another. If a man finds that his present occupation does not pay him well, he will leave it and enter some other vocation which is more profitable than before. In India the caste system has put a check to such kind of mobility. People hesitate to change one occupation for another of a lower grade, (though it is more profitable), because of their being born in a particular caste. There is also the requirement of the necessary skill of knowledge to change one occupation for another.

---

## CHAPTER IX.

### *INTEREST AND PROFITS.*

Interest is the money income which capital returns to its owner. Those who possess wealth do not consume the whole of it. After the necessaries and other

luxuries have been provided for, there remains with them a stock of wealth which they can conveniently use in lending others on a certain charge. They are required to wait or abstain from the use of that stock in order that they may earn an income on it. The income they derive is called interest. It is said that interest is the reward for abstinence. But abstinence suggests some sacrifice, and it can not be said that rich people whose income far exceeds their expenditure, practise abstinence in this sense. Marshall regards interest as the reward of waiting rather than of abstinence. Waiting implies postponement of consumption.

**Net Interest** When we say that interest is the reward for waiting simply for the use of capital we mean that it is the Net Interest. On the other hand we have Gross Interest which is composed of other elements besides the net interest. When we use the term interest in common language we generally refer to *gross interest* which is the whole amount which a person is required to pay by way of interest on the capital borrowed. Gross interest consists of two elements as payment to cover *risks of loss* and the *earnings of management*.

When a money-lender lends money to a borrower, the former has to undertake certain kinds of risks. One of these is that the borrower may not return the capital when it is due owing to some circumstances. In the case of buying and selling of commodities the transaction between the two parties is complete when the seller hands over the commodity in return for a certain fixed price. But

money lending is a transaction which extends over a considerable period of time and it is possible that during this period, the borrower may be made unable to repay the sum borrowed. The lender therefore guards himself against such risk by charging in every case something more than the net interest. "If we suppose that a man who has lent Rs 10,000 in sums to a large number of people, charges each of them two per cent to cover the risk, then he hopes to receive Rs 200 in a year in addition to the net interest. If he finds at the end of the year that all his capital is repaid, he has gained Rs 200, while if his debtors are unable to pay, say Rs 500 in all he has lost Rs 300 only" (Moreland). Much depends upon the credit of the persons who borrow money. If the credit of such persons is good that is to say if people generally expect them to pay their debts the money lender will not be very particular about the insurance against risk involved in making advances. If on the contrary, then credit is bad, the lender will exact from them a very high interest.

*Earnings of managements* These vary according to the trouble the lender is put to in ascertaining the surety of the agreement made by the parties. If there is a mortgage of property, he must find out whether it is legally valid or not. In many cases he has got with himself securities in the form of jewels, ornaments etc. He is to guard these things from being stolen away or otherwise.

From what has been said above we find that net interest is found out by deducting from the



charge actually made (gross interest, something on account of insurance against risk, and something on account of earnings of management)

**Rate of Interest.** Having considered the relation between Gross and Net Interest, we will now pass on to the factors that determine the rate of Interest. Here again we are to look at the demand and supply forces

The rule that is applicable to the value of commodities, also applies to the value (interest) of capital. There is a demand for and supply of capital.

**Demand** People generally demand capital because it has utility and it may be used in productive purposes. It will be seen that the majority of people need money for the latter purpose. There are other uses to which the borrowed capital is to be applied. People require capital for ceremonial purposes, house-building etc. The amount which a person will be induced to borrow will depend upon the rate of interest. If the rate be high, he will borrow less and vice versa. Suppose if a person can get a loan, say at 4 p c he will perhaps borrow 800 rupees and earn Rs 200 for himself after the interest has been paid. If the rate were increased he finds that he can hardly get anything for himself after he has paid the interest, and as a consequence of which, he will think it worth his while not to borrow.

**Supply** We have considered the causes of the accumulation of capital in a country. It will be enough to say that the accumulation of capital

is governed by a variety of causes, "by custom, by habits of self-control, and above all by the power of family affection security is a necessary condition for it, and progress of knowledge and intelligence furthers it in many ways" (Marshall). The fluctuations in the rate of interest affect the saving capacity of people to a great extent. When the rate is high many people are tempted to deposit their money in Banks or engage it in some other concerns. Thus a high rate of interest is in one way a healthy sign of a country's saving power. If the rate be low, no capital will come forward to be employed in productive purposes. But a person, who wishes that his family should get a particular amount of sum as interest on the capital which he is saving, will find in those conditions (low rate) that he is required to save more in order to get that amount of interest. Fall in the rate of interest may in a way help the accumulation of wealth.

The determination of the rate of interest will depend upon these forces of demand and supply. If there is a great demand for capital, it will be met for a time not by an increase in the supply but by a rise in the rate of interest. This rise will cause capital to withdraw itself from those uses in which the need for it is less urgent. If on the other hand the supply is greater than demand the rate would tend to be low. We will illustrate this by an example. If the rate were, say, 5 p.c. people will demand Rs. 40000 and the money lenders would be willing to supply 60000 Rs. If the rate were reduced to 4 p.c. people will demand 60000 Rs. while the money-lender will offer 40000 only.

After much bargaining on both the sides the rate would perhaps settle at  $4\frac{1}{2}$  per cent and Rs 50000 would be offered and taken. Thus equilibrium of demand and supply would be established.

*Mobility of Capital in India* It has been said that much of the capital in India has been hoarded by the people. The amount absorbed in hoarding is estimated at 500 and 800 crores of rupees. But this can hardly be the case. In old days it might have been true to say that the country absorbed much of her wealth in hoards, because there was no security and good Government to ensure safety of the property. There was an absence of facilities in the form of Banking. But this has been changed during recent times. With the growth of Banking and the advent of a strong Government, much capital is now brought forward to be utilised in profitable business. New industries are day by day absorbing a good deal of capital by giving dividends on the shares. The people have begun to appreciate the advantages of lending their savings to industrial and commercial concerns. In reality there is no great increase in the amount of capital invested by the people in the agricultural industry and other small handicrafts. But in the manufacturing industries, there is a remarkable development in this direction. Almost the whole of the capital of the cotton mills amounting to no less than twenty-five crores of rupees, has been raised in India. Still a good deal of foreign capital has been invested in many Indian Industries. The reason of this is that the expert knowledge and the organising capacity which are necessary

for the establishment of such concerns are practically absent in India. An exception has been afforded in this case by the establishing of the Tata Iron and Steel Company which was floated in 1907 with exclusively Indian capital of more than two crores of rupees. There is a good deal of capital still hoarded in the country, which may enable enterprising people to start new industries if they can attract it by inspiring confidence in the people.

*Cooperative Credit Societies.* Cooperation in its technical sense, means the abandonment of competition in distribution and in production. In distributive cooperation, the customers who are members of the cooperative societies select one of them as manager of the store, and share the resulting profit if any. As they are expected to make no purchase elsewhere, there is no competition. In productive cooperation, the object is to eliminate the capitalist and to remove competition between the workmen. The labourers elect one or more of their number to control the enterprise and divide among themselves the gain.

India is an agricultural country. Credit is an absolute necessity in all agricultural countries, and this is specially the case here. Indian agriculture is carried on a small scale and the poor agriculturist with his small plot of land has not got sufficient capital to carry his work on the field. He is therefore, compelled to seek the help of the village money lender who lends money on a very high rate of interest. Easy and cheap credit, however, has a great danger. It leads to excessive borrow

ing on the part of the agriculturist which would mean his ultimate ruin. The Government then thought of interfering in the matter of removing the indebtedness of the agricultural classes in the country. In 1892 Mr F A Nicholson was directed by the Madras Government to inquire and report on the possibilities of Agricultural Banking in Madras. He recommended to find societies on the lines of "Raiffeisen" which are rural banks formed by the person of that name. The principles of these rural banks are .—

- (1) Members belong to the same local area.
- (2) Unlimited liability of members.
- (3) No shares are issued
- (4) No dividends are distributed
- (5) Loans are granted for productive purposes only
- (6) There is no entrance fee.
- (7) Only the Secretary is the paid member

When the Government became fully convinced of the benefits that could be derived from such institutions, cooperative credit societies Act was passed in 1904. This Act divided the societies into (i) Rural and (ii) Urban. In case of the rural societies the principles of the Raiffeisen were followed. The Urban societies were founded on the principles of *Schulze-Delitzsch*. The principles of these type of Urban Banks are —

- (1) Members are drawn from a large area.
- (2) Large salaries are paid to the officers
- (3) Dividends are distributed
- (4) General banking is also done.

(5) They are not limited to the relief of the agriculturists alone.

The provisions of the Act were as follows —

(1) Any ten persons living in the same rural area or town or belonging to the same caste or class can form a society.

(2) The main business of the society was to raise funds by deposits from members and by loans from non-members.

(3) The management of these societies is put under the Registrar who audits the accounts of the Society.

(4) The liability of a member of a Society was to be unlimited in the case of rural Societies. In this case the terms limited and unlimited liability need some explanation. In a limited liability Society, the member is liable for the debts or losses only to the limit of his own share. While in an unlimited liability Society, he is liable for the losses of others. Thus if any loss occurred to the Society in the form of non-payment of debts by any member, then that loss would be equally divided among the members.

(5) No parts of the funds may be divided by way of dividend or otherwise among its members; the profits were to be carried to the Reserve Fund at the end of the year. In case of the Urban Societies, no dividend was payable until one fourth of the profit in a year was carried to the reserve.

### **Principles of Cooperative Credit.**

(1) The society was to consist of absolutely .

Profits will tend to increase if there is a decrease in the cost of production or an increase in the revenue. If the organiser got cheap labour and if he could get raw material at cheaper rates, it will reduce his expenses of production. But the prices he will charge will not be lowered to the same degree, hence there will be an increase in the income which goes to him in the form of profits. Secondly the income from a business will increase if the organiser manages his business more efficiently and if his produce is sold at higher price. The two together will bring about a rise in the amount of profits.

*Profits arise owing to the following reasons:—*

(1) A business organiser undergoes the expenses of production before the things are actually sold. In this respect he has to make rough calculations regarding the prices at which the produce will be demanded. If this calculations do not come out true, the business suffers a loss. He is therefore, very careful in making estimates. He usually calculates below the approximate point. In this case, he will have some surplus left to him in spite of the fact that other rival producers have attracted some of his customers by selling commodities at prices lower than he has.

(2) There are certain kinds of speculative risks present in the determination of profits. The organiser's contract with the other agents to pay them a definite sum, is based on the supposition that his produce will bring him a certain price. If he is right in the supposition he will certainly have some surplus which will go to him in the form of

profits. If he is wrong he will have to suffer a loss. Thus, a certain kind of risk is present in the calculation of profits.

(3) Thirdly there is an element of monopoly—some special advantage enjoyed by a producer over his rivals. Some producers have got peculiar advantages in the form of production on a large scale, better machinery, patent rights etc. The effect of these all is that they enable them to sell goods at whatever price they like. Again the expenses incurred by these producers will be less because they will enjoy all the advantages accruing to them on account of production on a large scale.

**Business opportunities in India** The natural resources of the country are so abundant that they can be utilized in nearly all the industries. But as it is, most of the raw materials and products are exported yearly to foreign countries whence they return in the shape of manufactured goods. It is quite recently that the Indians have begun to realise the advantages of cooperation and combination. The country is now utilising much of its raw cotton for manufacturing yarn and there are many mills and factories engaged in the cotton industry. Besides the raw materials, there are the minerals which can be extracted from the earth. These are coal, gold, petroleum and iron. Indian capital has not been much attracted towards such industries. It was only in 1907 that the Tata Iron and Steel Works were established with Indian capital. In spite of many opportunities afforded by the country, the fact still remains to be true that modern industry to be successful must be undertaken



by the educated Indian. But he lacks the practical common sense of the business man and his education has not filled him for the discharge of the multifarious duties of the modern entrepreneur. For this purpose educated young men must be equipped with sufficient scientific knowledge and practical training and a large class of men must arise who will be capable of taking upon themselves the responsibilities of business management. For the proper training of such business men, commercial training is quite essential. The course of studies ought to include subjects like commercial law and History, Banking methods, import and export problems, exchange rates and transport etc.

---

## CHAPTER X

### *CONSUMPTION.*

**Meaning of Consumption.** The word consumption is used in a general sense in common parlance. Whenever we consume a thing we say that it is used up and has ceased to be available. The amount of food that is consumed exists no longer to be used up again. But economics gives a somewhat restricted meaning to the word consumption. It is that part of the economic science which consists in the satisfaction of wants. A person can satisfy his wants only when he has got some income to spend over them. Thus, the satisfaction of wants and the spending of income are closely related to each other. The word consumption is sometimes confused with the word destruction. Hence the distinction between the two

should be carefully noted. Consumption is the removal of economic utilities by using them up, while destruction is the abolition of these utilities without using them. A shirt is said to be consumed when it is worn out by use, while it will be destroyed if it is burnt by fire.

When economists speak of things being consumed they mean that they have been used in the direct satisfaction of want. Food will be said to be consumed because it has satisfied some want. People generally purchase things in order that they (things) may satisfy their wants. Thus we find that just as man can produce only utilities, so he can consume nothing more, but utilities. For, the things which satisfy wants must possess utility or the power to satisfy want.

**Satisfaction as the end of all economic activity.** Some writers regarded the production of wealth as the cause of its consumption. But it is not so. The economic activity can be said to have begun only because men had wants. First of all man had wants and in order to satisfy these wants he had to make some effort. We have seen the relation of wants and efforts while studying the 'productive effort' in the second chapter of the present book. Wants and activities are interrelated. Although it is man's wants which gave rise to activities, yet afterwards each new step upwards is to be regarded rather as the development of new activities giving rise to new wants, than that of new wants giving rise to new activities (Marshall).

The more a person has, the more he will want.

Each time a fresh desire arises Every where there arise new wants to be satisfied If a person is doing a certain kind of work, he will think of new ways and methods of doing it more easily and in a better manner A person usually gets tired by the monotony in the mode of both work and living He therefore, wants some change. This change is brought over by the creation of new wants Thus, we see that the whole object of economic activity centres round the satisfaction of wants Wants giving rise to new activities which in their turn bring new wants It is therefore that consumption has come to be regarded as an important part of economics "It is in fact both its beginning and its end It is its beginning because the desire to consume is the motive of all economic activity Man has needs and he makes the effort which is necessary before they can be satisfied. It is its end because when the effort has been made, when the wealth has been produced, that wealth has no other function or purpose than to be applied directly or indirectly to the satisfaction of human wants." (Penson).

**Relation between consumption and production** Consumption is negative production. It is the removal of utilities. While production is the creation of economic utilities Production is nothing but a rearrangement of matter so as to make it more useful; while consumption is a disarrangement of matter so as to render it no more useful

There are some kinds of wealth which

satisfy our wants just as they are. While there are others which help us in the production of those things which we require for the satisfaction of our wants. The former class of things are said to satisfy our wants directly, while the latter indirectly. The former are called consumption goods, while the latter production goods. We have seen (while studying wealth) the distinction between these two classes of goods, hence it will be unnecessary to repeat it here.

The two processes of production and consumption go on side by side. A labourer who works for his living, is also consuming some part of the wealth, at the same time he is engaged in producing it. Every day fresh wealth is being produced but every day also wealth is being consumed; so that at the day's end, the total amount of wealth in existence is very much what it was in the beginning. Thus the two processes are interrelated.

There is no distinction between producers and consumers. The same person is a producer and a consumer. When a person renders some services to get an income, he is said to be a producer; while when he makes use of that income in satisfying his wants, he is said to be a consumer. Of course, a man will be benefitted as a producer when his income increases but at the same time he gets a greater command over the satisfaction of wants; i.e. he can buy more things than he used to do before. It may happen that an increased income would not bring in increased satisfaction. This is due to the fact that the cost

of living is also increased, we therefore see that a person's income plays an important part in yielding him satisfaction of his wants. A person will be induced to spend more only when his income has increased. As with the individual, so with the community. But in the case of the latter, satisfaction is not measured by income but by the output. In a community, there are many persons whose share in the produce may be increased without any increase in the whole output. This means that some persons are getting less {while others more. But the community as a whole can not consume more than it produces,

### **Wants and their Classification.**

Throughout the preceding pages, we have been using the word "wants". We will now consider what it means, and what kinds of want are there for the satisfaction of which all economic activity has been directed. It must be remembered that wants are very various and numerous. But we must confine our attention to only those wants which give rise to effective demand, that is to say, demand implying a determination to possess a thing and the willingness and means to have it. Thus wants imply an incentive to effort. Unless a man is prepared to do certain effort and to undergo some sacrifice, he will not have his wants satisfied. Mere desire to satisfy wants will be of no avail. Wants then, in the economic sense of the term are that effective desire for particular things which express itself in the effort or sacrifice necessary to obtain them. Economics is then concerned with all the wants to satisfy which a

man spends his income.

There is a variety of wants, some wants are more urgent than others, some are more durable. We may then study wants according to these various attributes

**Urgency.** Food, clothes shelter, these things constitute a large portion of the wants, of an ordinary man. But of all these wants, that for food is the most urgent. A hungry person will be ready to part with any thing for a morsel of food; so also in a desert the want for water is of the greatest importance. The other things *viz* light, clothing, shelter constitute wants of a rather less intensity. But they are urgent in comparison to other wants

**Attractiveness.** This class of wants depends upon the different tastes and temperaments of the people. Some prefer one thing to another simply, because they have a certain kind of interest in it. It is no doubt true that people are willing to pay more for such things than they would do in ordinary cases

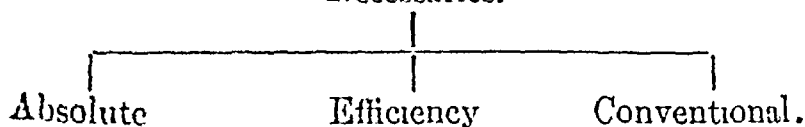
**Durability.** There are some wants, the satisfaction derived from which is a very brief one. While there are others which yield satisfaction for a long time. In the former class may be included things such as food, drink etc. In the latter class some things like houses, furniture, clothes etc. The real point of difference between the two is that in the former case the want recurs just after a short time, while in the case of house, furniture etc. it comes only after a long time, the

satisfaction derived from them lasting over a long period.

It is not possible for a person to satisfy all his wants. When such is the case, there must be some wants which would get first preference over others. According to the above classification, we can judge that those wants will be satisfied first which are urgent. The rest are satisfied according to the intensity of a person's mind to have them or not. He compares the marginal utility of one want with another, and satisfies that want first which yields him greater utility. A head of a family will first of all satisfy his urgent wants, and then will see which other wants are more intensely pressing on him. He also calculates the utility which he would derive by satisfying a particular kind of want in preference to another. When man is thus deciding how to spend his income there are some wants which he will arrange to satisfy before he thinks of providing for others, and the things needed to satisfy these wants are spoken of as *Necessaries*, while other things which he wants are called *comforts* or *luxuries*. Wants then are usually divided into (1) *Necessaries* (2) *Comforts* & (3) *Luxuries*.

**Necessaries.** These include things the wants for which must be satisfied. But here again a trouble arises. When we say a want must be satisfied, what are the consequences we have in view if it is not satisfied? In other words, are necessities the things which are necessary for life, or those which are necessary for efficiency? We are thus brought to a classification of *Necessaries*.

## Necessaries.



*Absolute necessities* include the things which a man must have in order to keep himself and his family alive. In other countries the term included, in addition to sufficient food and drink, a certain amount of clothing and also some sort of house for shelter, but in India the necessary amount of clothing and shelter is very small, and perhaps a blanket for the winter is all that an ordinary man requires. *Efficiency necessities* include more than this every thing that a man must consume in order to work efficiently at his occupation, and to educate his children upto the level he himself reached. Many people do not consume the necessities for efficiency, but they spend a relatively large share of their income on things other than that. The expenditure they incur is not for their efficiency, but they are forced to incur it by custom and by the power of public opinion. In India we find that much is spent on marriages and other religious functions. In fact, it is quite useless to incur this expenditure, but custom, the unyielding tyrant as Carlyle put it, requires that it should be so.

**Comforts and Luxuries.** In fact there is no real distinction between the two terms. Both denote things that are satisfied if there remains some income after the satisfaction of the necessities for existence and efficiency. Comfort usually



includes a moderate standard of living. When we speak of comforts, we mean the expenditure incurred on them, is more or less justifiable. While luxuries denote a more elaborate standard of living. When we speak of a man spending his income on luxuries, we simply say that in our opinion he is not making the right use of his income. It is usual to regard these two words as depending largely on the amount of income enjoyed by the person whose expenditure is being considered. The distinction is unimportant for the science of economics.

We have dealt with the law of Diminishing utility, and the total and marginal utility of a thing while considering the problem of exchange, we need not repeat them in this place. The only thing that demands our attention at this stage of our study is the expression consumer's surplus.

**Consumer's Surplus** People generally pay much less for a thing than the amount of the utility it yields to them. A person calculates in his mind the price he is usually prepared to pay for a thing rather than go without it. But it is often the case that what he actually pays never exceeds and seldom comes up to the maximum price. The satisfaction which he gets from the purchase of a thing generally exceeds that which he gives up in paying away its price. In this way he derives from the purchase a surplus of satisfaction. The difference between what he actually pays over what he would have been required to pay rather than go without the thing is called the *Consumer's surplus*. The consumer's surplus derived from some commodities

is much greater than that derived from others. There are many things the prices of which are very much below than what the people would ordinarily pay rather than go without them. In case of such things the surplus is very great. Instances of this kind are matches, salt, postage stamps etc. We are prepared to pay any price for these things, but what we actually pay is much below the maximum price we would have offered rather than go without them. Hence the difference between the two prices is the consumer's surplus from our point of view.

**The Marginal Utility of Money** Money like other commodities is said to possess utility, because it helps us to get our wants satisfied. But the value of money depends upon what it would purchase. The law of diminishing utility is also applicable to money to a small degree. With the increase in the amount of money a person has the utility of money diminishes. A rich person will not care as much for money as a poor man would. The marginal utility of money varies with different incomes. To a poor man 1 Re. means much more than it does to a rich. If the poorer man spends more he will suffer from the want of it afterwards than the richer would do.

**Division of income among different items of expenditure** The choice of a person to purchase a certain thing in preference to another depends usually on the cost to that thing and the degree of satisfaction which is got from consuming it. Some things will be cheaper, and other things rather dearer, and he will pay more for what is cheaper and little for what is dearer, but this deci-

sion in each case is based on the same consideration, the endeavour to obtain the greatest possible amount of utility in return for the money which he is able to spend. We will illustrate this by an example. Let there be four things ( articles ) which are consumed every day tea, sugar, milk, and butter. Let us also suppose that these articles can be bought as one unit for a rupee. It is certain that the utility of these articles will vary with every person. Suppose to a person the utility of these articles measured in an anna of the successive units of the articles in question is as follows:—

Of milk	...	30, 28, 24, 20, 16, 12.
Butter	...	26, 24, 20, 16, 12, 10.
Sugar	...	24, 20, 16, 12, 10, 8.
Tea	...	20, 16, 12, 10, 8, 6.

As each unit costs 1 rupee, it is evident that no unit will be bought the utility of which is less than 16 annas. Thus the person would buy five units of milk, four units of butter, three units of sugar and two units of tea. He has only fourteen rupees with him. He will distribute this in order of the degree of the utility he derives from the four articles. Thus the first rupee will be devoted to milk, the second also to milk, the third to butter, for the utility derived from the first unit on butter is greater than that derived from the third unit on milk and so on.

**Family Budgets.** From the above illustration it will be seen that different people with limited income distribute their purchases of necessary things with the consideration that they would get the

highest possible utility out of them. It is generally found that each and every family has got a rough budget which shows how its income is divided on different articles. Different countries have tried to make investigations as to how people with a given income generally distribute their expenditure. They have succeeded in finding out the results. The great statistician Dr Engel has compiled some careful statistics of the expenditure of the lower, middle and working classes in Saxony in 1857. From the tables given by him, it will be found out that as the income increases the proportion of it devoted to food diminishes, while a large portion goes to what may be called the comforts of life.

## CHAPTER XI.

### *SPENDING AND SAVING*

We have been considering up till now the satisfaction of wants. In order to satisfy wants, there must be income. It is difficult to get the whole of the income. Income is divided into (1) Personal and (2) Social. Social income consists of the claims of the state, and the claims of other religious bodies. Personal expenditure consists in (1) aiming at the immediate satisfaction of wants (2) aiming at the providing a store of wealth which will help the productive effort and will serve as a source of future enjoyment to those making it or their dependants. The former is generally known as spending, the latter as saving.

**Saving** The term saving has been associated

with the mistaken notion of hoarding. When a person keeps some money in hoards, people generally say that he has saved money. But this is not the meaning of the term from the economic point of view. In economics that part of wealth is purposely kept aside for being employed in production. Saving does suggest keeping aside money for the satisfaction of some future wants. The income which a person saves may be employed for some industrial or commercial purposes. In this case the man who saved the wealth does not use it for his own sake. He transfers it to others who can put it to a better and more profitable use. But this does not mean that the person who transfers this capital does not get any thing in return. As we have seen (while studying interest) he gets an interest on the capital which he invests or forwards. In this way his original income is increased. We have dealt with the causes which induce men to save. We therefore think it better not to repeat them again.

**Relation of Spending and Saving.**  
 Spending and saving have one thing in common. In both cases wealth is given in exchange for certain goods and services, but the difference is that goods and services are not put to the same use. When we consider them from the point of view of spending we find that they are applied in the direct satisfaction of wants. On the other hand, in the case of saving, they are applied for the production of other wealth which is an indirect satisfaction of wants. Thus we see that saving and spending are the two essential features of our everyday econo-

nic life. Wealth may be produced for the satisfaction of some future wants, because capital which is the result of saving helps the production of such wealth, and we know that capital is saved because it possesses the two attributes of prosperitiveness and productiveness. Some people are of opinion that wealth should not be saved, but should be spent as soon as we get it. Their object in this is that by spending more wealth will be put into circulation which will help to increase the commercial transactions. But they overlook the great need of the manufacturing classes and other producers of capital. If people do not save any wealth, but spend it, there will be no capital left for future production. This will decrease the output which will consequently raise prices. And with a rise in prices and income of the people remaining the same, people have less satisfaction to be derived from their income. On the other hand, it is quite erroneous to ask people to save instead of spend. The consequence of this will be that every body will try to utilize his income for productive purposes. But as there is a limit to the scale of production, a much increased output will hardly find way out to the market. Hence it is an unwise policy to apply one's income in saving rather than spending. It is quite essential that a person must spend some portion of his income, on the satisfaction of wants. A man of an ordinary common sense will balance future benefits against the present, and will so distribute his income between spending and saving, that he may be able to secure the greatest amount of satisfaction. Under normal conditions, economic force tends to adjust

this balance between spending and saving. If very little is being saved capital becomes scarce and the rate of interest rises. This increases the amount that can be enjoyed in the future and greater saving results. On the other hand, if people are saving too much, and capital becomes superabundant, the rate of interest falls, there is less in the way of future enjoyments to attract, and saving diminishes.

**The Social side of Spending.** Uptill now, we have been considering spending as measuring a particular amount of satisfaction to an individual. We will now deal it with reference to the Society consisting of individuals. The actions of individuals affect those of others. These actions are regulated by certain customs and regulations by which individuals are bound together in a community. As of actions, so of expenditures. It is not that the community regulates his expenditures. The law hardly interferes with a man's methods of spending his money so far as it affects only himself, but it does to a certain limited extent control his expenditure in cases where it is likely to be in actual conflict with the general interest. There has been a good deal of conflict of views regarding the state interference in this matter. But the most convenient and reasonable policy would be to let alone people to spend any thing they like, but should control such kind of expenditure as could be shown to be hurtful to the individual consumer or to other members of society. In India we find that there are certain restrictions put by the Government on intoxicat-

ing liquors, opiums, poisonous drugs etc Only those who are licensed to sell can keep the quantities of these articles with them. These restrictions have been imposed for the benefit of the Society at large

Every act of spending has its social side We demand a particular thing. It is this demand which in general leads many others to supply it. These people try to produce or procure what we want. Thus our wants influence others who produce the commodity for ourselves Just as the producers serve the consumers by supplying their wants, so the consumer has also a duty towards them. A consumer must not demand any thing in such a degree as would diminish the consuming power of the persons who supply his wants

---

## CHAPTER XII.

### TAXATION.

**Classification of Revenues.** Before we pass on to the consideration of the revenues of a state, we shall make a preliminary survey of the functions of Government. It is because of these that the Government raises revenue from its subjects. Every Government has to do some work for the benefit of the public which repays it in the form of revenue and taxes The income derived from these will vary with the nature of the services rendered by the state There are divergent views as regards the functions of a state. Some regard that the state should protect the individual against force and fraud. While other say, that



to the state should be delegated the regulation and control of practically every form of personal and social activity including the production and distribution of wealth. Now-a-days it has been regarded that the social well-being of the community is a matter of first rate importance, and that it is the duty of the State to promote it and to safeguard it as far as it possibly can. Having considered the functions of Government, we will come to the manner in which a Government obtains its income. This brings us to the consideration of the heading of this paragraph viz, the classification of revenues. The ways in which income is obtained by the state are various. The state revenue is derived from, (i) Taxation (ii) Property it possesses (iii) Services it renders (iv) Productive enterprise it carries on. The revenue derived from the fund, which peculiarly belongs to the sovereign or common wealth is known as Quasi Private revenue. Under this class come the posts and telegraphs, and mint, charges for services rendered by the state to particular individuals are of the nature of taxes. They include the fees for the conferring of the patent rights and payments demanded in the Courts of law. Revenue from the property includes the income derived from the crown lands.

### Revenue.

Quasi Private

Taxation.

- (1) Private property,
- (2) Services rendered by the state.
- (3) Post office, Telegraphs & Mint.

It will be better if we study this classification with reference to India. The revenue of the Government of India is derived from different sources. The classification of revenues in India closely resembles to the one given in the adjoining table. Here too a distinction is made between non-taxable and taxable revenue. The four parts of the revenue there are:—(1) the income derived from the possession of its own property e. g. lands, forests. (2) the profits of commercial undertakings e. g. Post office, railways (3) incidental gains from administrative departments e. g. the Law Courts, and lastly (4) taxation proper viz Contribution levied upon the people directly like the income tax and indirectly e. g. customs and excise duties.

### Revenue in India

<i>Non-taxable.</i>	<i>Taxable.</i>
(1) Private property,	(1) Direct.
(2) Profits of commercial undertakings	(2) Indirect.
(3) Incidental gains from administrative departments e. g. Law Courts etc.	

## TAXATION.

## THE TAX SYSTEM AND ITS INCIDENCE IN INDIA.

## Taxation.

---

Land revenue	Customs	Excise	Income tax	Death duties	Stamps.

---

"A tax" has been defined by Prof Bastable as "a compulsory contribution of the wealth of a person or body of persons for the service of the public powers". The definition would be clearly understood if we bear in mind what was said of the functions of the state and the income it derives. It is compulsory because it is enforced by law. Again there are the words "person" or "body" of persons. We know that every member of the state is required to pay taxes on consumable commodities, taxes in the form of land revenue, customs etc. Body of persons means companies etc. These are required to pay income tax and other taxes just as an individual does.

✓ Taxes are *direct* and *indirect*. Direct taxes are those which are collected from the individuals who it is intended or desired shall bear the burden of them e.g. the income tax, the land revenue, stamp duties and also licences which have to be taken out for carriages, motors, dogs, etc.

Direct taxes are collected from one person with the intention that he will get them back from some one else e.g. Excise duties i.e. taxes levied on the production or consumption of goods, and customs duties levied on goods brought into the country.

In one case a man cannot shift his tax on others, while in the other he pays a tax the burden of which he shall be able to shift on to others. We must note the two terms (1) *Incidence* and (2) *shifting* very carefully.

*Incidence* Where the burden of the tax actually falls is called its incidence. *Shifting*. The process of passing on the burden to some one else is called shifting.

Having dealt with these preliminary notions we will now turn to the taxation proper and its distribution.

*Distribution of taxation.* In order to understand the manner in which the burden of taxation is distributed we shall have to go to the four canons of taxation as set forth by Adam Smith.

(1) *Justice*. 'The subjects of each state ought to contribute towards the support of the Government as nearly as possible in proportion to their respective abilities, that is in proportion to the revenue which they enjoy under the protection of the state. In the observance or neglect of this maxim consists what is called the equality or inequality of taxation.

*Criticism.* Taxes should be apportioned according to the faculty or ability to pay. But it is rather difficult to measure this ability. Adam Smith tells us in the canon that it should be measured in terms of revenue. All property is not equally productive, and many persons with a little property have large incomes and therefore great faculty or ability to bear taxation. A rich person has no doubt greater ability to pay than a poor. Hence

it has been urged that the minimum should be exempt from taxation. It is considered at the present time that taxation should be designed so as to cause proportional real sacrifices among the tax payers. When such is the case, people are left in the same relative positions after being taxed as before. Equality in taxation is difficult to be attained because no one can ascertain definitely the amount each individual pays by way of taxes. This objection can be brushed aside by introducing the direct and indirect taxes. They balance this inequality. The former hardly fall on the people while the latter are shared by both to the extent to which they purchase the taxed commodity. The state takes more from the rich not because they will feel it less in proportion but because they have more to give.

(II) *Canon of certainty.* The amount to pay ought to be certain and not arbitrary, the time of payment, the manner of payment, the quantity to be paid all to be clear and plain to the contributor and to every other person.

This canon and the next two deal with the method of levying taxes. Now a days every body knows the amount, the manner and the time when the tax is to be paid. It should be said that this canon is aimed against the arbitrary exactions of the sovereign power and the jobbery and abuse of its officials.

(III) *Canon of convenience.* Every tax ought to be levied at the time and in the manner in which it is most likely to be convenient for the contributor to pay it.

It is necessary that the Government should collect taxes in the most convenient manner. It should not put both the contributor and the collector to any inconvenience. The Indian land revenue is collected according to the convenience of the cultivators.

(IV). *Canon of economy* Every tax ought to be so contrived as both to take out and to keep out of the pockets of the people as little as possible over and above what it brings into the state.

The Government should not spend more than is necessary for the collection of taxes. It should do so as economically as possible.

In addition to the above four canons of taxation, various other maxims have been added. It will not be worth our while to consider all of them. So we shall take only two.

(1) Taxes should be productive.

(2) Taxes should be elastic

Taxes are levied because the state wants to derive a considerable amount of income. Whether a tax is good or bad will depend upon the way in which it succeeds or fails to bring in good income to the state. Again, some new taxes are imposed against the will of the people. If such taxes did not serve their purpose, then there is no use imposing them under opposition. The advantages should compensate for the disadvantages in the form of displeasure and opposition met out in its imposition. Secondly a tax should not destroy or weaken the sources from which the money for the tax is derived, sometimes excess duties

instead of encouraging industries are an obstruction to them. Thus taxes would be unproductive because they would decrease the output of the industries and consequently the income derived from them.

Taxes should be elastic in order to avoid their extra imposition to obtain additional revenue. By elastic is meant that taxes can be increased without causing a falling off in the revenue derived from them. The Income tax has always been considered as one of the most elastic of taxes.

**Incidence of Taxation in India.** The only object of the Indian tax-system is the production of revenue. No attempt is here made to remove or modify through its systems of public finance any inequalities that may exist in the distribution of wealth among the different classes of society. The Government of India do not professedly accept any of the current theories of the appointment of taxation. In general the Government follows (1) the qualified proportional principle, in which income is taken as the standard and the amount of public burdens regulated by it, (2) and the progressive principle, which places a heavier rate of charge on large than on small incomes, since the ability of the tax payer is supposed to increase in a more rapid ratio than the increase of his income. The taxes in India are collected from a very large variety of sources. There are both the kinds of taxes here, *viz.* direct and indirect. The land revenue, the provincial rates (include cesses on land for roads, schools etc. and the assessed and excise duty are indirect.

*Income tax.* The income tax was first imposed in India in 1860 in order to meet the financial dislocation caused by the mutiny. It was levied at the rate of 4 p c. on all incomes of five hundred rupees and upwards. Since then there have been many changes. The last revision was in the budget of 1922-23 and the scale fixed is as follows :—

(a) In the case of every individual, every un-registered firm and every undivided Hindu family.

(1) When the total is less than	2000								Nil
(2) When the total is more than	2000 & less than	5000	5 pies per rupee						
(3)	"	"	"	5000	"	"	10000	6	" " "
(4)	"	"	"	10000	"	"	20000	9	" " "
(5)	"	"	"	20000	"	"	30000	1	ans. " "
(6)	"	"	"	30000	"	"	40000	1½	" " "
(7)	"	"	"	40000	"	"		1½	" " "

(b) In the case of every company and every registered firm whatever its total income, 1½ ans per rupee.

In respect of excess over 50000 rupees of total income a super-tax varying from one anna in the rupee to six annas in the rupee with the increase is levied

*Incidence.* According to the official calculations (1913) the incidence of taxes per head of population was Rs. 2-11-3 per year. If the land revenue is to be excluded, the burden would be Rs. 1-7-8. The proportion of taxation to the average income is nearly 9 p c. Very recently the incidence of taxation in India in 1922 was calculated to be at Rs 6 4-3 per head. This included land revenues, salt, stamps, excise, provincial rates, customs. Income per head is shown to be Rs. 20



according to Mr. Dadabhey's statement, and Rs 27 in 1881 according to Sir David Barbour's statement and Rs 30 in 1901 according to Lord Curzon's statement and Rs 50 in 1911 according to Mr. Cook's statement made on 23rd February 1921 in Council of State.

*Shifting of taxation.* In India there is no economic rent and a tax on rent may affect the prices of agricultural products and may be thus shifted on the consumers. Customs duties are shifted.

---

## APPENDIX.

~(1) Explain the subject matter of economics and discuss its relation to other sciences. PP. 1—2.

• (2) Explain “ Wants lead to effort and efforts bring satisfaction ” PP. 3—4,

• (3) What do you understand by production of wealth ? Distinguish between Capital and Wealth. P 5, 25.

• (4) What are the different stages of productive effort ? P 8

(5) What are the natural resources of India ? Show how they can be utilized. PP. 14—15.

(6) How do you account for the population of India being dense in some parts and sparse in others ? PP 18—19.

(7) Describe the system of irrigation in India. PP 21-22

(8) What determine the efficiency of labour ? Briefly state the condition of Indian labour. PP. 22—24

• (9) Explain what you understand by ‘ Division of labour.’ Give the advantages and disadvantages of division of labour. PP. 29—30.

(10) Explain “ Division of labour is limited by the extent of market ” P. 33.

• (11) Write notes on :—(a) Law of Diminishing Returns. (b) Value—Relative. (c) Supply

and stock. (d) Demand and Supply curves (e) Productivity of labour. (f) Marginal and Total Utility PP 8, 12-13, 39-40, 36.

(12) State and explain the law of Demand.  
P. 41.

(13) How is exchange by barter effected?  
P. 36

(14) What do you understand by the elasticity and inelasticity of Demand? PP. 41-42

(15) Explain how exchange value is determined in the market. P. 37.

(16) What are the principal Imports and Exports of India? PP. 44-46

(17) What are the qualities of a good metallic money? State the functions of money.  
PP. 46-47

(18) Explain :—(a) Mintage and Seignorage. (b) Debasement and Depreciation. (c) Bimetalism and Monometallism PP. 51-52.

(19) Distinguish between Convertible and inconvertible paper currency. State the disadvantages of the Inconvertible Paper Currency. PP. 53-54.

(20) Describe the machinery by which payments to foreign countries are made. P. 56.

(21) Explain briefly :—(1) Council bills, (2) Reverse Councils, (3) Gold Standard Reserve. (4) Gold Exchange Standard. (5) Home charges.  
PP. 59-60

(22) State the functions of banks. Explain the composition of Indian Money market giving briefly the development of Indian Banking. PP. 64—66.

(23) How does the problem of Distribution arise? P. 67.

(24) Define Rent and explain how it arises. Show whether the law of rent is applicable to India. Explain "Rent does not enter into the cost of production" PP. 71—77.

(25) How are wages determined? Distinguish between Real and Nominal wages. P. 79.

(26) What are the factors that determine the mobility of Labour? How far is Indian Labour mobile? P. 86.

(27) Distinguish between Gross and net Interest. How is the rate of Interest determined? PP. 88—90

(28) How are Co-operative Societies organised in India? What are the advantages arising out of them? PP. 93, 96.

(29) Analyse profits and show how they are determined. PP. 97—98.

(30) What is the relation between Production and Consumption? PP. 102—103.

(31) Classify Wants. PP. 104—105.

(32) What meaning is attributed to Spending and Saving in Economics? Is there any relation between the two? PP. 111—112.

• (33) What are the functions of the State? How does it classify its revenue? PP. 115—116.

• (34) Define Tax and explain the four canons of Adam Smith. PP. 118—121.

• (35) Distinguish between (a) Direct and Indirect Taxes (b) Incidence and Shifting of a tax PP. 118—119.

• (36) Explain the incidence of Taxation in India. PP. 122—123.

END.

